

PN-AAX-017

Viet Nam Terminal Report

Volume 1

A Summary

BEST AVAILABLE

BEST AVAILABLE

# Volume I, Viet Nam Terminal Report

I wrote this volume with the exception of the section entitled "An Economic Overview of South Viet Nam,

I had less to do with Volume II, which was written and edited by other members of the staff.

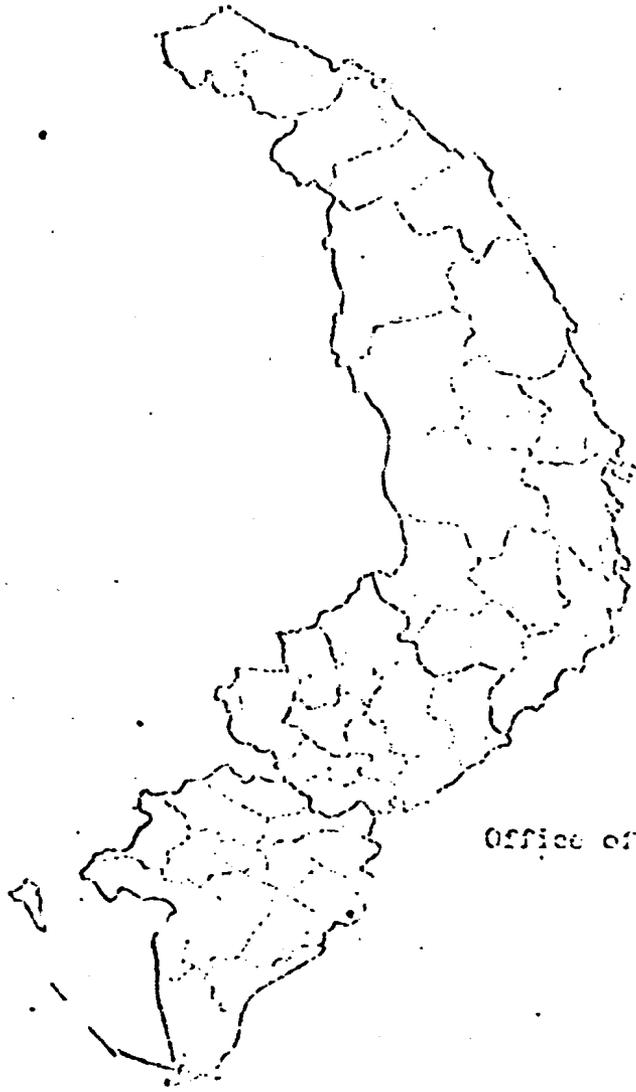
Volume III, the Bibliography, was conceptualized and supervised by me. It is made up entirely of official U.S. files and documents. It offers an unusual feature in that it gives the user the exact location of each item. This makes retrieval much easier.

Robert V. Craig Sr.

Return To:  
Robert V. Craig Sr.  
C/FFP, Rm 6212 NS

# United States Economic Assistance to South Vietnam • 1954-75

Volume I  
A Summary  
Part I



Prepared by the  
Asia Bureau  
Office of Residual Indochina Affairs  
Viet Nam Desk

December 11, 1975  
US Agency for International Development  
Washington, D.C.

## THE SCOPE OF THE TERMINAL REPORT

The Terminal Report, United States Economic Assistance to South Viet Nam, 1954 - 1975, consists of three volumes; the Summary which is contained in Volume I and II and the Bibliography of Official Documents in Volume III. The Summary provides the reader with a description of major economic assistance activities undertaken by the United States Agency for International Development and its predecessors during the extended period of U.S. involvement in South Viet Nam. It also serves as a factual account of the times as they pertained to U.S. programs and provides a setting for those who wish to read more fully by using the Bibliography. The Bibliography is an annotated listing of many of the major documents, files, reports, and other official records accumulated by the Agency over a period of more than 20 years.

This terminal Report was prepared in recognition of the magnitude and duration of the Agency's assistance to South Viet Nam. The report's purpose is to preserve primary source material of historical value.

Two other major activities were conducted as adjuncts to the Terminal Report:

1. Project Appraisal Reports of all ongoing A.I.D. projects at the time of the fall of the Government of Viet Nam have been prepared. These formal evaluation documents provide detailed information on the status of ongoing programs at the time of the fall.
2. A comprehensive description of economic policies and settings, the "Economic Context" has been prepared along with more detailed sector descriptions in certain areas, which provide supplemental information to the material in Volumes I and II of this Report.

Neither the Project Appraisal Reports nor the more detailed sector descriptions have been published, but copies are on file with the A.I.D. Reference Center, Agency for International Development, Washington, D.C. 20523. Both categories of unpublished documents are listed in the Bibliography under their respective subject headings.

## INTRODUCTION

The United States Government provided economic assistance to the Republic of Viet Nam (South Viet Nam) from its inception under the Geneva Accords of July 20, 1954 until its fall on April 30, 1975. These efforts are summarized in Volumes I and II of this Terminal Report, and Volume III provides the reader with an extensive bibliography for further research.

During much of the Viet Nam experience, U.S. economic aid was unlike any other effort with respect both to magnitude and to types of activities. In terms of objectives, the U.S. thrust in economic assistance may be divided into five periods:

1954-1958 - Separation of South Viet Nam from the Associated States of Indochina and an influx of refugees from the north to the south provided a series of immediate problems for the fledgling Vietnamese government. The following were some of the specific A.I.D. objectives aimed at easing some of those problems:

1. support efforts to reorganize and train a national army adequate to maintain internal security and provide initial resistance to external aggression;
2. help maintain economic stability and assist in rehabilitation and development efforts, including integration into the economy of the two million or more refugees, displaced persons and demobilized soldiers who might otherwise be vulnerable to communist subversion;
3. assist in strengthening and improving the structure and effectiveness of the government, so that it might become more responsive to the needs of the people;

4. help expand and improve public information services in order to increase popular understanding of and support for the government.

1959-1961 - Care of refugees was de-emphasized during this period inasmuch as refugee problems had been largely brought under control by 1958. The year 1958 was a time of transition from an emphasis on the task of helping to establish a new government to economic development. However, development attempts were increasingly thwarted from 1959 on, as the strength of the Viet Cong became evident.

1962-1966 - Economic assistance objectives changed dramatically during this period. Major emphasis was placed on counterinsurgency. Evolving objectives during this period were:

1. maintaining economic stability;
2. assisting Vietnamese Revolutionary Development efforts (pacification) to establish, expand and consolidate government control and services in the villages;
3. relieving the economic and social consequences of military operations;
4. expanding the economy in secure areas and preparing for future social and economic development.

1967-1972 - The transfer of pacification activities from USAID to the American military and the formal start of Vietnamization marked further shifts in U.S. goals during this period. USAID still played a supportive role in pacification, striving to ease the sufferings of war victims, and continuing its efforts to maintain economic stability. USAID stressed the development of Vietnamese institutions and services in the economic, social and technical assistance areas. The latter included both the capacity

for development planning and actual progress in development insofar as wartime conditions permitted.

1973-1975 - Policy shifts during 1973-1975 were dictated by Hanoi's Easter offensive of April 1972, the signing of the Paris Accords in January 1973, and declining real aid levels brought on by the combination of U.S. force withdrawal and worldwide price inflation. USAID priorities during this time were to:

1. meet the humanitarian requirements brought on by the increased hostilities, particularly in the area of refugees, but also children and others uprooted by the war;
2. assist in the transformation of the economy from a condition of external dependence to one of self-sufficiency.

This Summary depicts the setting in South Viet Nam under which these goals were developed, describes the U.S. responses in line with these goals, and attempts to show the rationale behind these responses.

U.S. economic assistance to South Viet Nam is summarized on the following page. Part A of the Table shows aid totals for each of the periods discussed above. Part B presents the same data in terms of annual averages.

#### A Definitional Note

Omitted from the aid summary are the piaster purchases of the U.S. sector which generated some \$2.6 billion of dollar earnings for the GVN during the course of the U.S. involvement. Piaster purchases fell into one of two general categories: (1) official purchases, which derived almost entirely from Military Assistance Support Funding (MASF) and financed the

local currency expenditures of the Military Assistance Command Viet Nam (MACV); (2) personal purchases, which financed the personal piaster expenditures of the U.S. military and civilian personnel (N.B.: official expenditures of the U.S. civil sector were financed almost entirely by counterpart generated by the Commercial Import Program.)

That piaster purchases were not aid funds in origin is therefore clear. What has been less clearly understood is that, for the most part, they were not aid in their effect. This is because the expenditures related to them consumed local resources--i.e., wage payments to local employees, rentals, payments to local contractors, etc.--for the benefit of the U.S. sector. The bulk of the expenditures fell into that category.

Certain piaster purchases were properly considered as aid. The significant programs in this category were DOD-financed highway programs funded under the so-called "AID/DOD Realignment Program," support of the Rural Development (RD) Cadre program and the Local Procurement Program (during 1971-75). They have not been included in the aid category partly because of insufficient data on the amounts involved. Moreover, while these programs were aid in the true sense of the term, at least two of them, the R D Cadre program and the Local Procurement program which involved the purchase of locally produced goods for transfer to the Vietnamese armed forces, were as much military as economic in nature. As an indication of their relative importance, the R D Cadre program involved a maximum of \$20 million in any one year; the AID/DOD Realignment program amounted to \$17.4 million in 1973, which was either the peak year in terms of expenditures or very close to it; and the Local Procurement program reached a

peak of \$28.6 million in 1973. These programs accounted for as much as two-thirds of a greatly reduced piaster purchase total during 1973-74, but no more than 10 percent of the total during years prior to 1972.

Direct Dollar Support for Humanitarian Aid under the so-called "Kennedy Amendment" during fiscal years 1972-75 fell into yet another category. Humanitarian Aid was a line item within the A.I.D. Appropriation for Viet Nam; hence, clearly aid. Yet because the funding mechanism (at the Viet Nam end) was identical to that of Defense Department operations requiring local currency purchases, it was included more often than not in piaster purchase summaries. The aid table below does include this Direct Dollar support on an obligations basis under "Project and Other Aid." Balance of payments tables within the ECONOMIC OVERVIEW Section show this funding on a receipts basis as a separate line item.

One further reservation needs to be made concerning the non-inclusion of piaster purchases within the aid tables. While the bulk of such purchases was not aid, the share of purchases made at an unrealistic exchange rate was, properly considered, aid. That is, to the extent the United States paid more for the piaster than it was worth they were supplying a form of grant aid. The amount of such "hidden aid" cannot be determined any more than the "true" value of the piaster could be determined. It was substantial--probably exceeding \$200 million--in certain years, especially during 1968-70 when the piaster was heavily overvalued. After 1971, when the piaster remained at or near a realistic level, the amount of "hidden aid" was insignificant. In any event, the aid table understates

a

the total amount of U.S. economic assistance to the extent that such "hidden aid" took place.

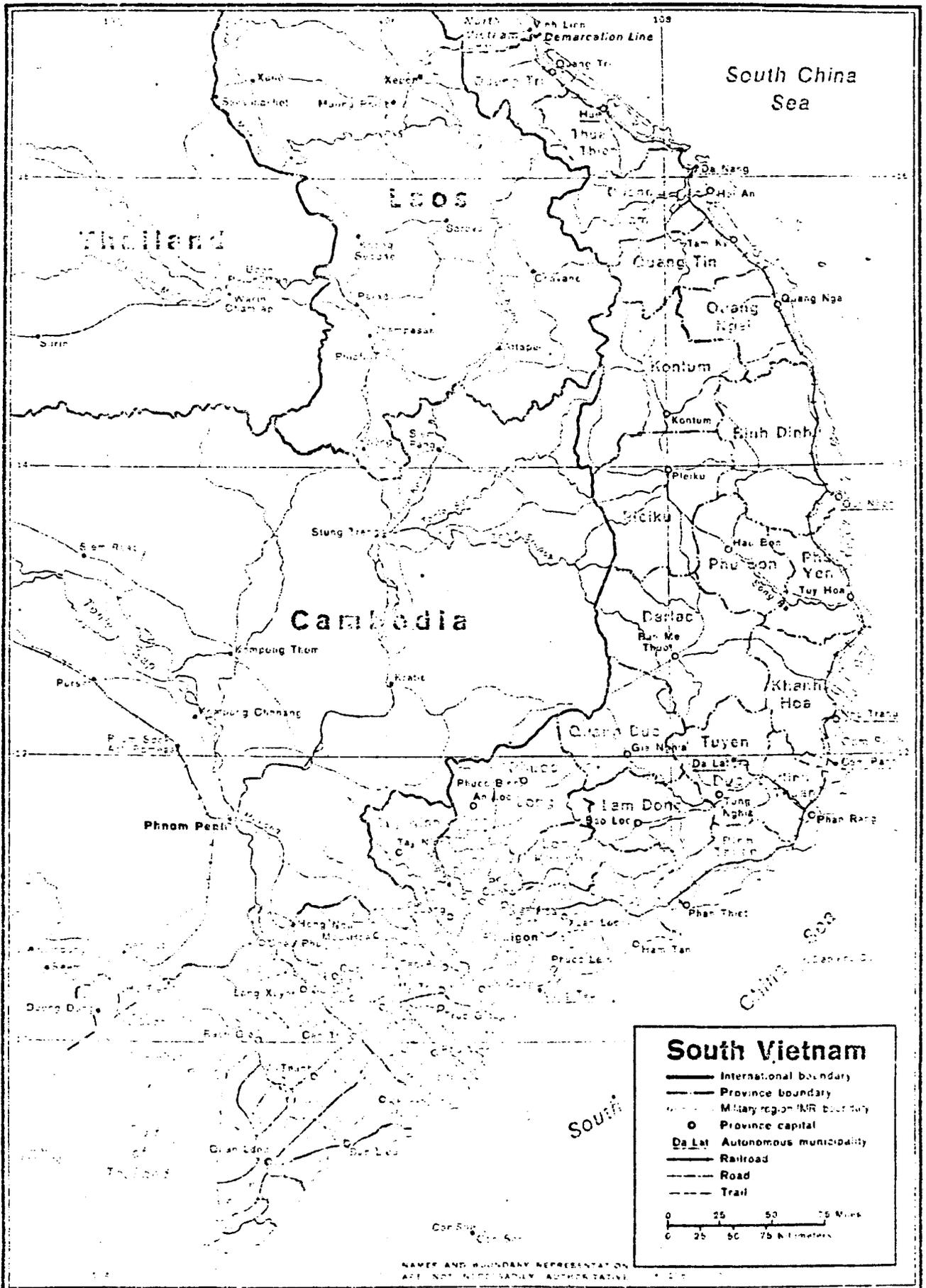
Piaster purchases, whether aid or not, did convey dollars to the GVN and were a crucial item in Viet Nam's balance of payments. Piaster purchase totals are properly included as a part of U.S. Import Support, a summary of which appears in Table 1 of the ECONOMIC OVERVIEW Section. They also appear in the Balance of Payments summary, Table 9 of the same section.

U.S. Economic Assistance to Viet Nam  
(Obligations Basis, Fiscal Years, in \$ Millions)

<u>Period</u>	<u>CIP</u>	<u>Food For Peace</u>	<u>Project and Other AID</u>	<u>Total</u>
<b>A. <u>Totals</u></b>				
1954-58	791.2	49.0	163.5	1,003.7
1959-61	393.2	29.3	118.7	541.2
1962-66	851.4	336.5	400.2	1,588.1
1967-72	1,282.6	678.2 <sup>a/</sup>	1,064.5	3,025.3
1973-75	<u>704.5</u> <sup>b/</sup>	<u>507.8</u> <sup>a/</sup>	<u>180.5</u>	<u>1,392.8</u>
Totals	4,022.9	1,600.8	1,927.4	7,551.1
<b>B. <u>Annual Averages</u></b>				
1954-58	158.2	9.8	32.7	200.7
1959-61	131.1	9.8	39.6	180.4
1962-66	170.3	67.3	80.1	317.6
1967-72	213.8	113.0 <sup>a/</sup>	177.4	504.2
1973-75	<u>234.8</u> <sup>b/</sup>	<u>159.3</u> <sup>a/</sup>	<u>60.2</u>	<u>454.3</u>
Totals	182.9	72.8	87.6	343.2

Notes: (a) Includes Direct Dollar Support for humanitarian aid totaling \$2.4 million in 1972 and \$86.3 million during 1973-75.

(b) Includes Program Loan of \$50 million in 1974.



12

TABLE OF CONTENTS

UNITED STATES ECONOMIC ASSISTANCE TO SOUTH VIETNAM, 1954-75

TERMINAL REPORT

Volume I - A Summary, Part 1

Viet Nam in Perspective

A general Overview

An Economic Overview of South Viet Nam

Rural Development & Field Operations

Volume II -- A Summary, Part 2

Agriculture

Child Care

Civil Aviation

Commercial Import Program

Development Planning

Education

Housing & Urban Affairs

Industry

Land Reform

Logistics

Public Administration & Labor

Public Health

Public Safety

Public Works

War Victims, Relief and Rehabilitation

Volume III - A Bibliography of Official Documents

Volume I

A Summary

Part 1

Viet Nam in Perspective

A General Overview

An Economic Overview of South Viet Nam

Rural Development & Field Operations

VIET NAM IN PERSPECTIVE

The Vietnamese people possess a history which is dominated by conflict from without and from within. They were either at war with the Chinese or under Chinese domination from the Third Century, B.C., until 946, A.D., when the final attempts of the Chinese to retake the Red River Delta were repelled. Although Viet Nam fell briefly once again into Chinese hands in the fifteenth century, A.D., it generally managed to maintain its independence until the French moved in and gradually claimed all of Indochina as a colony between 1858 and 1900.

The practice of westerners furnishing military support and advisors to the Vietnamese dates back to the sixteenth century, when the Portuguese helped the Nguyen faction of Viet Nam in its war with the Trinh faction. This activity came to a halt at the end of the seventeenth century when the Nguyen and Trinh factions reached a truce.

The French joined the Portuguese, the Dutch and the English in a fierce competition for trade in Viet Nam. By the early nineteenth century, the French had begun to dominate western influence, assisting Emperor Gia Long in overthrowing the Tay Son Dynasty and importing missionaries who played an important role in the subsequent relationships which developed between the French and the Vietnamese. Toward the middle of the nineteenth century, pressure was mounting in influential French quarters for positive action to establish a position for France in Viet Nam of the kind other European powers enjoyed, or were acquiring, elsewhere in Asia. The missionaries had been roused to an angry militance by the imprisonment or execution of some of their number and by the periodic persecution of Vietnamese Christians. An imperial ban had not halted missionary activity

in the country, but it was clear that local authorities would never cease to obstruct Christianity unless forced to do so. Consideration of French national prestige and military advantage were also present, as was the desire for a share of the economic benefits to be gained from an aggressive policy in Asia.

In September 1857, all these factors led to France's decision to take Tourane (Da Nang). The city was captured in 1858, and the French, thereafter, turned their attention to the south. Inflicting heavy losses on the Vietnamese, they took Saigon by July 1861. In June 1862, the Vietnamese court at Hue ceded Saigon and adjacent area to France and agreed to pay a war indemnity. They also promised not to cede territory to any other power without French permission. The western part of the Southern delta, which was virtually cut off from the rest of Viet Nam, was annexed by France in 1867, thus completing the territorial formation of what later became the French colony of Cochin China. The French next turned their attention to the Red River, having found the Mekong unsuitable as a trade route to China because of its rapids. A treaty was signed in 1874 which opened the Red River to French traders, but Chinese pirates largely nullified the value of the concession. In 1883, an expeditionary force brought northern Viet Nam under French control, and the signing of a Treaty of Protectorate on August 25, 1883 formally ended Viet Nam's independence.

The treaty of 1883 and one of June 1884 established French protectorates over northern Viet Nam (Tonkin) and central Viet Nam (Annam). All of southern Viet Nam (Cochin China) had been in French hands since the conquest in 1867 and now, with the abrogation of what was left of the

17

country's independence, the name "Viet Nam" itself was officially eliminated. In Annam, the emperor and his officials were left in charge of internal affairs, except for customs and public works, but they functioned under the eye of the French who had the right to station troops in the area. The protectorate over Tonkin made few concessions to the appearance of autonomy, and French resident officers in the larger towns directly controlled the administration. The final phase of French consolidation was marked by the formation of an Indochinese Union in 1887. Consisting of Tonkin, Annam, Cochin China and Cambodia (a French protectorate since 1883), the Union was administered under a French governor general who was responsible directly to the Ministry of Colonies in Paris. In 1893, Laos, following annexation by France, was also added to the Union.

The basic political structure of French Indochina was completed by 1900. Each of Viet Nam's three regions was treated differently, although basic policy decisions for all usually originated in Paris. Cochin China was administered directly by a French-staffed civil service under a governor and a colonial council. It also sent a representative to the Chamber of Deputies in Paris. The colonial council, the legislative body, consisted of both French and Vietnamese members. In the administrative apparatus, only subordinate positions were open for Vietnamese. In the protectorate of Tonkin, the mandarinat was retained for administrative purposes, but important executive powers were vested in a French senior resident at Hanoi. In Annam, where the emperor was still nominally in power and the mandarinat continued to function, French rule was only a little less direct.

Early in the twentieth century, nationalist movements began to develop, initially, among urban intellectuals. A number of nationalist groups found inspiration in the Chinese nationalist movement. Of these, the best known and most important was the Viet Nam Nationalist Party (Viet Nam Quoc Dan Dang--VNQDD). It was established first in 1925 in Canton. Two years later, the VNQDD was also established secretly in Hanoi by Nguyen Thai Hoc, a school teacher. An uprising staged in 1930 at Yen Bay, northwest of Hanoi, was severely repressed by the French. The VNQDD was nearly destroyed, and many of its surviving members fled to Yunnan in southwest China. They returned to Viet Nam after World War II to confront both the French and the communists. After the Yen Bay insurrection, the leadership of the clandestine nationalist movement in Viet Nam was taken over by the Indochinese Communist Party (Dong Duong Cong San Dang), which chose not to participate in that uprising. Formed in Hong Kong in 1930, it united several existing independent communist groups under the leadership of Nguyen Ai Quoc (Nguyen the Patriot), later known as Ho Chi Minh.

The thoroughness with which the Yen Bay uprising was repressed for a time rendered the more militant nationalists inactive. Some Vietnamese did, however, attempt to advance the cause of national liberation through reforms from above. They looked to the young Emperor Bao Dai as their best hope. Bao Dai had ascended the throne in 1925 at the age of 12 on the death of his father, Emperor Khai Dinh, but did not return to Viet Nam until 1932 after he had completed his education in France. Bao Dai was greeted with enthusiasm by the Vietnamese who expected that he would be able to persuade the French to install a more liberal regime. He attempt-

ted to reign as a constitutional monarch, according to the terms of the treaty of 1884 establishing the protectorate, and he strove to modernize the ancient imperial administration at Hue.

Among his young collaborators was Ngo Dinh Diem, governor of the Phan Thiet area in Binh Thuan province, who was given the portfolio of minister of the interior and appointed head of the secretariat of the Vietnamese-French commission which was charged with the responsibility of implementing Bao Dai's reform proposals. When it became obvious that the French had no intention of granting real power to the Vietnamese administration and would make no concessions toward unification of the country, the youthful emperor appeared to lose interest, and Ngo Dinh Diem resigned his official position.

After the fall of France in June 1940, the Vichy government acceded to Japanese demands, which ultimately led to the establishment of Japanese controls over all of the French Indochina peninsula. The Japanese occupation and the French reaction to it had the effect of further stimulating nationalist sentiments. Fearing that Japan would capitalize on the strong anti-French feelings of the people, the French administration undertook to liberalize certain of its repressive policies. It improved technical and vocational education programs, opened new schools, and launched a youth movement, presumably, in hopes of winning the support of youth groups. It also opened additional civil service posts for the Vietnamese. The French apparently intended, however, to reinforce the colonial order through these token concessions while they continued to impose restrictions on nationalistic activities.

Nguyen Ai Quoc (Ho Chi Minh), a communist since 1920 and founder of the Indochinese Communist Party in 1930, was still in the forefront of the Vietnamese communist movement ten years later, although he spent much of this period outside of Viet Nam. Allied with and deftly exploiting the non-communist nationalist groups, Nguyen Ai Quoc eventually emerged the dominant political figure of the country. To broaden the social and political bases of its activities, the Communist Party, in May 1941, adopted a policy of collaboration with all non-communist nationalists. This decision led to the formation of a united front organization, the Viet Nam Independence League (Viet Nam Doc Lap Don Minh), better known as the Viet Minh. One of the first actions of the Viet Minh was to form guerrilla bands, under the direction of Vo Nguyen Giap, to operate in Vietnamese territory against the Japanese and the French. He also began implanting agents and setting up intelligence networks in Tonkin. Meanwhile, efforts by non-aligned, non-communist groups, beset by factional wranglings, were virtually nonexistent. While in China, Ho Chi Minh was jailed for his communist activity in 1942. Nevertheless, the Viet Minh continued its vigorous efforts to win popular support.

During the same period, the Chinese, who urgently needed intelligence on Japanese activities in Tonkin, attempted to make use of the non-communist Vietnamese exiles for this purpose. At Chinese urging, a new organization called the Revolutionary League of Vietnam (Vietnam Cach Mainh Dong Minh Hoi, but usually abbreviated to Dong Minh Hoi), was formed in October 1942 and given financial support by the Chinese Kuomintang. Although all the major nationalist groups--including the Vietnamese Nationalist Party and Viet Minh--were represented in it, the new organization, without active

21

Viet Minh cooperation, remained ineffective. It was against this background that in 1943 the Chinese released Nguyen Ai Quoc in exchange for his offer to help them. Thereupon he took the name of Ho Chi Minh (He Who Enlightens), presumably to conceal his communist affiliation from the Vietnamese people.

Ho Chi Minh was expected to work through the Dong Minh Hoi and used the funds which the Dong Minh Hoi received from the Chinese Nationalist Government to strengthen his communist organization. His organization produced some intelligence of use to the Allies, and Vo Nguyen Giap 's guerrilla bands engaged in minor forays against the Japanese. In return, Ho Chi Minh received an undetermined amount of small arms, munitions and communication equipment from the United States for counteraction against the Japanese. This aid later formed the basis for his claim that the Viet Minh enjoyed Allied support. Working in nationalist disguise, Ho Chi Minh effectively strengthened the organization of communist cells throughout Viet Nam. In the subsequent struggle for leadership in the nationalist movement as the war ended, the superior organization of the communists enabled him to gain control of the Viet Minh and to claim the credit for nationalist activities during the war. Capitalizing on the burgeoning anticolonialist sentiment of the time, Vietnamese communists claimed to be fighting against economic misery and for national liberation.

In September 1944 the Tokyo government, alarmed over growing indications of anti-Japanese activities, decided to displace the French and grant independence to the Vietnamese. Initially, this plan was to be executed on April 25, 1945, but the reoccupation of the Philippines by the United States forces in October 1944 and the growing awareness that Japan was losing the war advanced the date of the Japanese displacement of the French,

- 225

and on March 9, 1945, at the instigation of the Japanese, Emperor Bao Dai proclaimed the independence of Viet Nam under Japanese "protection". Meanwhile, at Hanoi, the Viet Minh went into action, refusing to support the Bao Dai regime. Ho Chi Minh began to refer to the Viet Minh guerrilla units as the "National Liberation Army" and announced the formation of a Committee for the Liberation of the Vietnamese People, with himself as president. By late August 1945 the Viet Minh partisans and agents gained administrative control over the Tonkin area by a show of force. Bao Dai, apparently convinced that a united and independent nation offered the only possibility of preventing the return of French control, decided to abdicate. Recognizing only the nationalistic character of the Viet Minh movement and assuming that it had Allied support, he abdicated in its favor on August 25, 1945 and handed over his imperial seal and other symbols of office to Ho Chi Minh.

On September 2, Ho Chi Minh formally proclaimed the country's independence and the establishment of the Democratic Republic of Viet Nam.

At the Potsdam Conference of July 1945, the Allies agreed that the British were to accept the surrender of the Japanese south of the 16th parallel, and the Chinese would perform a similar duty north of it. After World War II the Vietnamese expected the Allies to support their claims to independence. Nationalist China opposed the return to France of Indochina, <sup>hoping</sup> apparently to reassert its traditional influence over Tonkin, and, in principle, the United States favored the formation of a provisional international trusteeship. <sup>However,</sup> in February 1946, a Franco-Chinese agreement was concluded whereby China agreed to withdraw from the northern area. An agreement between France and Ho Chi Minh was signed in March 1946, by which the Democratic Republic of Vietnam was recognized as a "free state" within

the Indochinese Federation (yet to be created) and the French Union. As a result of this agreement, French forces were permitted to land in the north. Bao Dai, who had been acting as high counselor to Ho Chi Minh, was sent on a "goodwill" mission to China where he remained in exile, thus eliminating the possibility that he might provide a rallying point for groups not thoroughly aligned with the Viet Minh.

Differences between the French and the Democratic Republic of Viet Nam immediately developed over the question of defining the "free state". A delegation of the Vietnamese representatives, headed by Ho Chi Minh, traveled to Paris to settle differences. The Paris Conference was broken up in early June 1946 when a Republic of Cochín China was established in the south with the support of separatist French elements. In September 1946, however, Ho Chi Minh signed a modus vivendi on behalf of his government-- an agreement which he reportedly described as "better than nothing". The agreement was designed to facilitate the resumption of French economic and cultural activities in return for French promises to introduce a more liberal regime. The modus vivendi did not include recognition of Vietnamese unity or independence and was opposed by many within Ho Chi Minh's regime. French actions to enforce customs controls in October aroused further hostility. In November shooting broke out in Haiphong, and the subsequent French bombardment of the city reportedly killed more than 6,000 Vietnamese. The French demands which followed were so completely unacceptable to the Democratic Republic of Vietnam that it decided to risk a long war of liberation rather than to accept. On December 19, 1946, it launched the first attack on the French in what was to be known as the Indochina War. In this act of resistance against French troops, the Republic had the active or passive support of a majority of Vietnamese.

24

The war touched off by the Viet Minh attack lasted for eight years and caused unending misery to the Vietnamese as well as the French. It was financially and militarily disastrous to the French and resulted in more than 35,000 of them killed and 48,000 wounded. The United States gave the French substantial military and economic aid in support of their Vietnamese efforts, reportedly totaling over \$2 billion during this protracted period. Large sums were also spent by communist China and the Soviet-bloc countries on assistance to Ho Chi Minh's regime. The war, which started out as an anti-French struggle, became enmeshed with the worldwide conflict between East and West. During this period, the Vietnamese people also witnessed the emergence of two governments, both competing for popular support.

In the early months of 1947, the French military forces reestablished their control over the principal towns in Tonkin and Annam and cleared the road between Haiphong and Hanoi. This forced the Viet Minh to resort to the guerrilla tactics which became the chief characteristic of the war. Ho Chi Minh's armed forces made use of the jungle to neutralize French mechanized mobility and power. By selecting their objectives and retiring when they met superior strength, they presented a problem with which the French could not cope. After three years of fighting, the Viet Minh controlled large areas throughout the country. The French had firm control only in the large cities.

Early in the struggle, the French sought to encourage the Vietnamese anticommunist nationalists to take a stand against the Viet Minh and to cooperate with France, but the effort failed as the nationalists claimed

the French would not clarify their policy with respect to future Vietnamese unity and independence. In 1946 some of the anticommunist nationalists in Nanking, China, formed a Front of National Union of Vietnam and appealed to Bao Dai to return from exile in Hong Kong and head a national government. The French, seeing another opportunity to make the nationalists an effective counterforce against Ho Chi Minh, offered Viet Nam "liberty within the French Union". Bao Dai, apparently fearful of becoming a pawn of the French, cautiously agreed only to represent Viet Nam in negotiations. Violent Viet Minh reaction to these maneuvers included the assassination of prominent nationalist leaders. Negotiations between the nationalists and the French continued for two years and by June 1949 France finally approved the limited independence for "the State of Viet Nam" within the French Union. Bao Dai assumed the role of chief of state, but the principal nationalists (including Ngo Dinh Diem) failed to unite behind him, since they claimed that the French did not offer real independence. Although the new government was permitted internal autonomy and an army of its own, strong safeguards to protect French nationals and economic interests were maintained, and the foreign policy of the new state was coordinated with that of France.

In the meantime, Ho Chi Minh rid his coalition government of the moderates and nationalists whom he had accepted earlier and showed himself to be completely communist. In March 1951 the Indochinese Communist Party (dissolved in 1945) was revived as the Workers Party (Dang Lao Dong). Propaganda emanating from the government, however, continued to be solely nationalistic in tone.

After the defeat of the Chinese Nationalists by the communists in late 1949, Communist China became the first state to recognize the North

26

Vietnamese regime as the legitimate government of all Viet Nam. Soviet-bloc countries quickly followed suit. In early 1950, after North Viet Nam began to receive assistance from Communist China, offensive action was accelerated against the French Union forces composed of Vietnamese as well as French soldiers. In 1951 the advance of the communist forces was temporarily halted with the aid of American equipment, but in 1952 the communists started a new offensive in several areas. Vigorous counter-attacks brought no decisive results, and a military stalemate followed; where tanks could go, the French Union forces held, but in the mountains and in the mud of the rice paddies Ho Chi Minh consolidated his control.

In February 1950, Great Britain and the United States recognized the State of Viet Nam headed by the ex-emperor Bao Dai as the legitimate government. When France concluded agreements with Laos and Cambodia similar to that with Viet Nam, the three countries became the Associated States of Indochina and were accorded diplomatic recognition by more than 30 other nations. In May 1950 the United States announced a decision to give aid to Bao Dai through France, and a United States Economic Mission arrived in Saigon. In September 1951 a United States-Vietnamese agreement for direct economic assistance was also signed.

The Bao Dai regime was unsuccessful in its efforts to win popular support. Confronted with a choice between French colonialism and the communist led nationalist movement, many Vietnamese, attracted by its appeal for independence and unity, tended to side with the Viet Minh organization. While the military battle was raging, steps were being taken to bring a negotiated end to the Indochina War. France was admittedly unable to continue the war and Ho Chi Minh, under apparent Sino-Soviet pressure, had let it be known that he was ready to discuss peace.

In February 1954 the Big Four (France, Great Britain, the Soviet Union and the United States) powers at Berlin agreed that a conference should be held to seek a solution to the Indochina War as well as the one raging in Korea.

On April 28, 1954, two days after the opening of the conference at Geneva, a Franco-Vietnamese (nationalist) declaration, proclaiming Viet Nam to be unequivocally sovereign and independent, was made public. It was only after May 8, however, that the conference began focusing its attention on all of Indochina. The immediate cause was the decisive French defeat at Dien Bien Phu at the hands of the Viet Minh forces on May 7 and the resultant popular pressure in France for a rapid conclusion of the war. The Indochinese phase of the conference was attended, under the co-chairmanship of Great Britain and the Soviet Union, by the representatives of the United States, France, the United Kingdom, the Soviet Union, Communist China, the State of Viet Nam, the Democratic Republic of Viet Nam, Cambodia and Laos. Final negotiations for armistice were conducted directly between the French High Command and Ho Chi Minh's People's Army High Command. A truce agreement covering the territory of both North and South Viet Nam was signed on July 20 between the two High Commands. Separate truce agreements were also concluded for Cambodia and Laos, respectively.

The agreement for Viet Nam fixed a provisional military demarcation line roughly along the seventeenth parallel and provided for total evacuation from north of the demarcation line of the military forces of France and the State of Viet Nam, as well as for the evacuation of the Viet Minh forces from south of the demarcation line. It also provided for a period of 300

days during which freedom of movement was to be allowed for all persons wishing to move from one sector to the other. Under the agreement, the introduction into Viet Nam of any troop reinforcements and additional military personnel was prohibited except for rotation purposes; imports of new weapons were similarly limited to replacement levels. It also imposed restrictions on the establishment of foreign military bases, and on the participation of both North and South Viet Nam in any military alliance. Finally, the agreement provided for the formation of an International Control Commission, with representatives from India, Canada and Poland, to supervise the implementation of the truce arrangements. In addition to the agreement, a Final Declaration, dated July 21, of the Geneva Conference provided for the holding of general elections throughout North and South Viet Nam in July 1956 under the supervision of the International Control Commission with preliminary discussion to begin in July 1955.

The armistice agreement was reached over the objections of the State of Viet Nam which did not sign it. It vainly protested the manner in which the truce was arranged, as well as its terms, particularly those relating to the partitioning of the country. It demanded that the whole country be placed under the control of the United Nations until conditions warranted the holding of free general elections. It also objected to the Final Declaration, protesting that the French High Command arrogated to itself, without prior consultation with the State of Viet Nam, the right to fix the date for elections. The United States also did not concur with the terms of the truce agreement or with the Final Declaration. In a unilateral statement issued on July 21, however, the U.S. representative declared that his country would refrain from the threat or use of force to disturb the provisions of the agreement and of the Final Declaration and that

29

it would view any renewal of aggression in violation of the agreement with grave concern as a threat to international peace and security. With regard to the provisions relating to the elections, the United States expressed its continuing determination to seek unification through free and fair elections to be conducted under the supervision of the United Nations. It further reiterated its traditional position that all peoples are entitled to determine their own future and that it would not join in any arrangement which would hinder the realization of such a principle.

France then proceeded to complete the transfer of the remnants of its administrative and military control to the State of Viet Nam with its capital at Saigon. The government of Ho Chi Minh, seated at Hanoi, moved steadily to achieve its program of communizing north of the seventeenth parallel. Despite the cease fire agreement, a well organized Viet Minh underground network was left behind in the south, especially in the jungle regions in the southern Mekong Delta and along the Cambodian and Laos border regions where French Union forces had not been able to establish effective control. This underground network formed the nucleus of subsequent Viet Cong insurgency directed against the Saigon regime.

A GENERAL OVERVIEW

Shaping a New Country: 1954-1958

Signing of the Geneva Accords in July 1954 set the South Vietnamese Government adrift from the traditional organizational structures which had guided its banking system, its foreign policy and its educational, agricultural, and public health systems. Experienced French administrators and technicians who advised previous governments were leaving. Communist activities, although clandestine, continued. The Vietnamese civil administration was weak and the national army disorganized. The Chief of State, Bao Dai, called on Ngo Dinh Diem to form a government but, although Premier, he lacked control, especially over the army. In addition, three powerful sects, each with its own army, formed opposition to the Diem government. After a time, Diem brought the army under control and after six months eliminated serious opposition from the Binh Xuyen, one of the sects threatening the stability of the new government. Fighting against the other two, the Cao Dai and Hoa Hao, continued for some time before it was contained.

Diem turned his attention to his own status and called for a referendum to allow Vietnamese to choose between Diem and Emperor Bao Dai. A referendum was ordered for October 23, 1955, and Diem's bid to replace Bao Dai was successful. Official Vietnamese government records showed that 97.8 percent of the voting population participated and that 98.2 percent of the voters chose to replace Bao Dai with Diem as Chief of State. Refusing to recognize the provisions of the Geneva Accords which called for the holding of general north-south elections in 1956, Diem proceeded to form a legislative branch of the government in the south.

A constitution was drafted. Election of a 123-man unicameral National Assembly was held on March 10, 1956. Amidst charges of rigged elections, Diem had succeeded in setting up both the presidency and the National Assembly in an effort to strengthen the central government.

During this tumult of warring factions and political turmoil, the U.S. economic assistance community attempted to help the new government with some of the concrete problems it faced in institutional development, refugee care and resettlement, and training of administrators and technicians for the public service. The United States, which had been providing military and economic assistance to Viet Nam

through France ever since World War II, had established its first economic mission in Saigon in 1950. This office, designated as the Special Technical and Economic Mission (STEM), operated in cooperation with the French, providing assistance to the Associated States of Indochina, including North Viet Nam. This mission, which was essentially of a technical assistance nature, was limited both in scope and in funds.

Signing of the Geneva Accords prompted the establishment of the United States Operations Mission (USOM) in July 1954 to deal exclusively with the problems of the newly created Government of South Viet Nam (GVN). The new country was beset by numerous problems which created, in turn, new demands upon the U.S. economic assistance program. The first and most urgent human problem to be dealt with was the arrival of nearly one million refugees from North Viet Nam within the first 300 days of the South Vietnamese government's existence.

At the time the number of refugees was based at more than 800,000 (see Attachment 1) but later indications suggest there may have been in excess of 900,000 refugees. Those who moved from South to North Viet Nam numbered about 90,000, including Viet Minh cadre and their families.

The refugees from the North, whose travel and subsistence were provided by USOM under its program "Operation Exodus," had been transported and housed in reception centers in the South. The massive operation cost \$55 million, including \$11 million for a U.S. Navy sealift. By FY 1956, with a budget of \$37 million, the refugee effort concentrated on resettling the new arrivals from reception camps to designated villages, which had been surveyed earlier to test their economic potential. Through the Commissariat General for Refugees, USOM provided funding for specific projects in these villages to allow the refugees to reestablish themselves as farmers, artisans and small businessmen. The refugee operations were largely completed by mid-1957.

In addition to meeting the immediate refugee problem, USOM, and its parent agency, the Mutual Security Administration, saw Viet Nam's situation and its major problems in 1955 as:

1. Internal and External Threats. Groups opposing the Diem regime still posed a threat to survival of the government. Even though Diem had made progress in quelling and pacifying some of these groups, only an uneasy truce left the government in a controlling position. Viet Cong activity was seen also as a threat to the new government. Then there remained a potential threat from the North.

2. Economic Problems. South Viet Nam's budget receipts and foreign exchange earnings were far below its expenditures, which were inflated by the cost of maintaining a large army and the cost of providing minimal assistance to refugees. Exports covered only 20 percent of necessary imports. Hence, the bulk of the country's imports were dependent on foreign aid. There was a need to improve both the productive capacity and the living conditions of a people weary from years of war. The threat of inflation was present. And there was a lag in the formation of new governmental economic and financial agencies to replace those established by the French for the Associated States of Indochina. The shift in economic assistance from mostly French franc aid to direct U.S. dollar aid created opportunities for competition and hence lower prices for the Vietnamese. But new trade relationships and procedures between importers and non-French suppliers were slow to develop.

3. War Victims. There were more than two million persons left displaced by the war, including the refugees from the North. Nearly a million South Vietnamese had been displaced by the war and needed assistance in order to resume normal existence. Demobilized soldiers and their families added to the social problem for the government. And all of these groups presented a potential source of unrest to discomfort the government.

4. Administration. USOM felt that South Viet Nam's civil administration required strengthening in order to improve and extend government services and increase operating efficiency. The added responsibilities

of independence made this need particularly acute.

The Mutual Security Agency outlined four objectives in Viet Nam at the time:

1. Provide financial support for the reorganization and training of a national army adequate to maintain internal security and provide initial resistance to external aggression.
2. Assist in maintaining economic stability and in rehabilitation and development efforts, including integration into the economy of the two million or more refugees, displaced persons and demobilized soldiers who might otherwise be vulnerable to communist subversion.
3. Assist in strengthening and improving the structure and effectiveness of the government, so that it might become more responsive to the needs of the people.
4. Help expand and improve public information services in order to increase popular understanding of, and support for, the government.

In keeping with these objectives, USOM's 1955 and 1956 programs were developed to support development of the army, mainly by providing funds to defray costs of pay and allowances, training costs, construction, and military medical services. Relief and resettlement of refugees from the north, as well as displaced persons in the south, received priority attention as well. Assistance was also given in agriculture, land reform, irrigation, agricultural credit, transportation, and public health but these areas received less attention during this period than in later years. Experts were provided to establish a new national bank,

improve central bank operations, foreign exchange and related fiscal operations, taxation, budget formulation and foreign trade policy. A number of contract American employees were brought to Viet Nam to advise in improvement of the overall administration of the government. And USOM continued a 1951 project directed at development of government information facilities and began a second project in 1956 to develop a national radio network, both activities aimed at achievement of the fourth objective described above.

A sizeable commercial import program was generated in order to attain the second objective, i.e. economic stability, and to generate local currency in pursuit of other objectives.\* During its first year as a separate nation, 1955, the national budget amounted to 537 million dollars. Revenues totaled 146 million, leaving 73 percent gap. The Commercial Import Program, which essentially filled the gap, brought goods into the country which were sold for piasters. The piasters so generated, known as counterpart, were given to the Republic of Viet Nam to cover budgetary outlays.

USOM created a Trade Division in April 1955 to handle the burgeoning Commercial Import Program. The program was utilized as a major tool for economic stabilization throughout the course of U.S. involvement and in every year, excepting the period 1967-69, was the largest single A.I.D. program in terms of monetary input.

\*The Commercial Import Program was a continuation of a similar program, which had been used by USOM's predecessor, to generate piasters for Viet Nam during the French Indochina War.

In FY 1955, \$322 million in economic assistance was provided by the U.S. The Commercial Import Program, providing capital goods and raw materials of value to the economy, accounted for \$254 million, or 79 percent, of the total. Most of the counterpart funds were attributed to support of military programs. Refugee and technical assistance accounted for 18 and 9 percent, respectively, of the total program.

The budget deficit was narrowed in 1956, to \$392 million from \$537 million the year before. Ordinary revenues covered 48 percent of expenditures compared with 27 percent in 1955. USOM's assistance was accordingly reduced from \$322 million in FY 1955 to \$210 million in FY 1956 of which the Commercial Import Program accounted for 83 percent.

USOM operations shifted gradually from stabilization and refugee assistance during 1954-55 to programs of technical and economic assistance aimed at modernization of the government apparatus and the economy. By mid-1958, emergencies had been contained and peace was a temporary reality.

USOM began to concentrate on a program of economic and technical assistance aimed at helping Viet Nam regain economic stability, improve its agricultural production, improve revenue collections, and restore its badly damaged and neglected physical infrastructure, as well as train administrators and technicians. Total economic assistance for FY 1958 amounted to \$189 million and cumulative economic aid from 1954 through 1958 totaled a billion dollars.

USOM direct hire personnel grew from 27 in 1955 to 164 by 1958. Most of these employees were technicians, such as agriculturists, educators and medical specialists; in addition, there were numbers of Americans working in Viet Nam under USOM contracts, addressing specific technical problems. This number increased from one in 1955 to 342 by 1958.

USOM had developed 42 joint projects with the Vietnamese government in support of its overall goals by mid-1958. These projects were distributed in seven major areas: agriculture and natural resources, 11 projects; industry and mining, 4; public works, 11; health services, 3; education, 6; public administration, 5; and information, 2. Details of USOM aid projects are discussed in later sections of this report. (For listing of projects, see Attachment 3.)

#### The Rise of the Viet Cong: 1959-1961

A sustained effort against communist subversion appeared to have reduced that disruptive force by early 1959 and more land was being put into production.

USOM was expanding its technical assistance efforts during this period and had 48 active projects in South Viet Nam in 1959. There were 16 institutional contractors active, including the Michigan State University team which had been engaged in advisory work in government and police administration since 1955. The number of direct hire employees stood at 199.

In 1957, the Government of Viet Nam began a land development program to reshuffle families living in overcrowded areas into areas where land

was plentiful, but not yet developed. Most of these land development centers were in the sparsely populated mountainous Highlands of South Viet Nam. USOM allocated VN\$ 350,000,000 for land development in 1959 and 45,000 people were resettled, bringing the total since 1957 to 125,000. By 1960, 121 villages accommodating 159,000 farm people had been established. This program continued until 1963 and received mixed reaction as to its effectiveness. Some progress was made in industrialization and the railroad was reopened from Saigon to Dong Ha, near the 17th parallel. Rice production in 1959 reached five million metric tons, more than twice the 1954 level. Rice exports reached a post-Indochina War high of 245,000 tons. In general, conditions appeared more conducive for stability and growth than for some time.

In late 1959 the Viet Cong began to increase terrorism, although not with sufficient impetus to disrupt either USOM or GVN programs to a significant degree, as it would do later. In fact, Viet Nam made substantial gains in agriculture, education, and industry during 1960. Through its agricultural assistance, USOM aided the Vietnamese government in raising the yield of rice paddy from 1.9 tons per hectare in 1956/57 to 2.2 tons in 1959/60. But it also gave great emphasis during this period to crop diversification in a country which was heavily dependent on rice and rubber. USOM also played an important role in developing Viet Nam's educational system which had been badly neglected during the war years. As a result, elementary enrollment stood at 1,500,000 on September 1, 1960, a surprising increase from only 400,000 four years

-40

before. There were many positive progress indicators in 1960. And progress continued in a number of key areas as late as 1963 and 1964.

By late 1960, the Viet Cong insurgency was becoming a serious issue. The U.S. Government was aware of the growing problem and Vice-President Lyndon Johnson, visiting Saigon in May 1961, promised to increase aid to South Viet Nam. President John F. Kennedy decided to increase military assistance to the beleaguered country and by 1962 USOM was engaged in executing civil programs designed to assist the Vietnamese Government to deal with the insurgency.

The era of relative peace was coming to an end. The high hopes of peaceful development, which were engendered by the formation of a free South Viet Nam in 1954 and by moderate successes in the development field since, were also fading. From 1961 on, USOM shifted its operations from those of stabilization and peaceful development to the realities of a period of war which would continue, except for one relatively peaceful interlude from 1969 to 1971, until Saigon fell on April 30, 1975. However, the momentum of development did not abruptly stop in 1960 or 1961. Rice production, only 2.8 million tons of paddy in 1955, reached 4.9 million tons six years later, in 1961, and 5.2 million in 1963. The country continued to show gradual progress even though it was clear that an insurgency of growing proportions had sprung from the isolated terrorist activities of 1959.

41

An Era Of Counterinsurgency: 1962-1966

In 1962, USOM shifted emphasis from its traditional role in economic development to one of civil counterinsurgency as the entire U. S. mission began to focus on the growing insurgency, which by that year had become a serious threat to the stability of the Vietnamese government. It may be useful to review some of the events in Viet Nam from 1954 to 1962 which led to this new direction.

The end of the French Indochina war in 1954 suggested that peace might logically follow in its footsteps. But there was a certain amount of communist activity from the beginning which hinted, at least in hindsight, of the greater violence to come. By 1959, it became clear that the Viet Cong were stepping up violence to some degree in the south. However, the direct response to guerrilla warfare did not fall within the specific nor the traditional considerations of U. S. economic assistance programs. Responsibility for response lay with the South Vietnamese government and from the U. S. side with the Military Advisory Assistance Group (MAAG). In 1960 the U. S. MAAG helped the Vietnamese Army form sixty Vietnamese ranger companies trained for antiguerrilla warfare. Later in the year, MAAG prepared an organized pacification plan. This plan was not placed into execution but similar plans would follow in later years from these early beginnings.

In addition to the fact that the insurgency was growing, there were also signs that certain elements of the Vietnamese population were

42

becoming dissatisfied with the leadership of President Ngo Dinh Diem, especially the Buddhists who claimed the regime was unduly repressive. There was an unsuccessful coup in December 1960 and the dissatisfaction between President Diem and elements of the population would grow for three years until November 1963 when he was deposed by another coup and killed.

On December 12, 1960 the Viet Cong formally announced the establishment of the National Front for Liberation and terrorist activity continued to rise.

#### U. S. Revises Objectives

In Washington an interagency Viet Nam Task Force was formed under the State Department and included representation from the Defense Department, A.I.D., the U. S. Information Agency (USIA) and the Central Intelligence Agency (CIA). Two study missions were dispatched to South Viet Nam in 1961, one led by Eugene Staley and the other by General Maxwell Taylor. Both groups called for political and administrative reforms, new economic programs for rural areas, greatly increased U. S. advisory and supply efforts and a larger, more effective Vietnamese military establishment. Those areas dealing with economic programs and administrative reform would provide the basis for A.I.D.'s involvement in counterinsurgency as it developed in the early 1960s. Both A.I.D. and the Military Assistance Advisory Group began enlarging their staffs. MAAG had doubled its size in 1960 to 685 advisors and leaped to 10,000 advisors by the end of 1962. By December 1962, USOM and MAAG had advisors at the province level throughout South Viet Nam. For A.I.D. this represented the second time it had fielded officers at the province level but in 1962 the mission was

43'

quite different than that of the 1954-58 period. Now it was targeted specifically on the civil aspects of counterinsurgency with the hamlet, the lowest administrative level of government, emphasized as the basic recipient of assistance programs managed and monitored from the province level. (See attachment 4 for a chart indicating the various echelons of government administration.)

This shift in direction was not universally heralded within A.I.D. There were those who felt that only those activities which normally fell under A.I.D. operations should be conducted in Viet Nam. The prevailing argument, however, was in favor of initiating short-term civil counterinsurgency programs which would stave off defeat and enable more traditional approaches to development after the threat against the Government of Viet Nam had diminished. The thrust to maintain economic stability, mainly through the tool of the Commercial Import Program, continued through the 1962-1966 period. But in the area of project assistance, there were major shifts toward shorter-term political and security objectives.

At the Saigon level, USOM created the Division of Rural Affairs (redesignated the Office of Rural Affairs in June 1962) to command its counterinsurgency field operations. This altered the USOM staffing pattern considerably, placing a large element of A.I.D. officers in the area of field operations with sub-offices established in Viet Nam's four military regions as well as in the provinces. By 1964 the Office for Rural Affairs (ORA) and the Office for Program and Planning were designated

44

as the two main offices of the USOM organization. ORA ostensibly coordinated the work of the technical divisions and provided counterinsurgency and project assistance with emphasis on counterinsurgency. The long range goal of this effort was to gain the support of the rural people for the government of Viet Nam. The program office provided economic expertise, program planning assistance and nonproject economic assistance, including the Commercial Import Program which remained in terms of dollar input the largest U. S. aid program in Viet Nam. (See Attachment 5.)

During this period, USOM public health programs were phased from advisory interests in preventive medicine to an expanded program of direct medical care for sick and wounded Vietnamese. U. S. and other country medical teams, including physicians as well as support personnel, were stationed at province hospitals. Education programs were redirected from long-range goals to short-term rural programs aimed at gaining political support. The hamlet classroom became a primary target and thousands of such classrooms were built in the ensuing years as a result of these new directions. Agriculture shifted to large operations designed to distribute fertilizer, introduce more productive rice strains, and generally improve rapidly the income of farm families which constituted the major segment of the nation's population. The refugee effort was boosted with increased advisors, commodities and funds to meet the humane as well as political pressures brought on by large scale movements occasioned by increasing warfare. Another major thrust was the development of a modern logistics system for the Government of Viet Nam. USOM supply advisors

45

were stationed eventually as far afield as the province level in efforts to bring quicker results.

During this period, USOM became the principal advisor to a Vietnamese program, Chieu Hoi, which was originated to encourage Viet Cong to defect and rejoin the GVN. The Chieu Hoi program, translated "Open Arms", was based on similar programs undertaken during the Malayan and Philippine insurgencies and provided Viet Cong with a more desirable alternative to surrender, which would have led them to prison camps. A Viet Cong who reentered society through the Chieu Hoi program received 45 days indoctrination in a special camp set up in his province capital, and was then free to rejoin his family. The GVN reported 11,248 returnees in 1963. After the fall of President Diem in November, 1963, the program faltered for two years with fewer than a thousand returnees each year, but picked up steam once again after 1965, reaching its zenith in 1969, surpassing its goal of 40,000 returnees.

USOM began directing more attention to the National Police in 1962. As the Michigan State University police advisory contract expired USOM's public safety division began gearing up for the task of developing a national police system which could handle not only those elements of law enforcement which are normally associated with police work but also to deal with those aspects of counterinsurgency in which the police would be expected to play a major role. Programs during this period included establishment of an extensive radio communications system to assist police in making contact with and serving larger segments of the rural

-46-

population. The Public Safety Division estimated that the GVN police force of 17,000 in 1962 was not nearly the size needed to provide law and order in rural as well as urban areas and assisted the National Police in training additional officers with which to expand the force.

By 1964 there were 58 direct hire police advisors in South Viet Nam. During the coming years this number would increase many times as the public safety program extended its advisory effort to each province in South Viet Nam. Total aid dollar funding for National Police grew from \$265,000 in FY 1955 to \$3.5 million in FY 1962 and rose sharply to \$20.7 million in 1966 as USOM expanded both its program support and its technical staff. By May 1, 1967 the National Police strength had reached 65,700.

#### The Strategic Hamlet Program

The GVN, which had suspended village elections in 1956, began a program of local development in 1959 known as the Agrovillage program, which essentially was an attempt to build social and economic centers. This plan was discontinued in 1961, primarily because of its unpopularity with the residents who had been moved into them, and the Vietnamese began experimenting with the "strategic hamlet" concept. The decision to concentrate pacification strategies at the hamlet, the lowest administrative unit, rather than the larger village level, hardened during this period. Not until 1969 did the Vietnamese and their American allies conclude that the village level was the more profitable level for government attention. Hamlet pacification without utilizing the village structure presented a

47

formidable problem in that there were between 10,000 and 12,000\* hamlets (as compared to some 2,100 villages) in Viet Nam, a number which required more personnel and material support than the government, even with general American support, could muster.

The GVN provided vastly inflated figures to the U. S. on the progress of the strategic hamlet program, which constituted the basis of counter-insurgency activities through 1964. By November 1963 the GVN claimed 8,544 strategic hamlets had been completed and another 1,051 were under construction. But the figures proved invalid, with less than half this number even nominally completed.

On the afternoon of November 1, 1963, military forces organized under General Duong Van Minh, seized strategic points in the City of Saigon and called for the surrender of President Diem and his brother, Nhu. By the following day, Diem and Nhu had been seized and executed. The national government was paralyzed by the fall of South Viet Nam's first president.

The death of President Diem sealed the fate of the strategic hamlet program. During the months following his demise the pacification program remained stagnated for the balance of 1963 and through 1964, although there was an enormous amount of activity spent in planning new

---

\*Although Viet Nam counted 12,000 hamlets in 1962, there were a number of factors which obscured an accurate assessment, including the fact that some hamlets which had ceased to exist, were still carried on official rolls. Later, more direct attempts to assess hamlets led to the conclusion that there were about 10,000 existing hamlets.

-48

approaches to counterinsurgency during 1964.

The Struggle to Reestablish the National Government

From November 1963 until the installation of Premier Nguyen Cao Ky on 19 June 1965, a plethora of governments attempted to rule South Viet Nam, some lasting only a few days or weeks. Animosities developed over whether the government should be military or civilian. Buddhist factions stirred in protest of military government but the strength of government during this period was directly related to the Army which represented the prime political force of that time. After a succession of generals and civilians had held the office of premier, it finally fell to Air Marshal Ky, who held power until 1967. National elections in 1967 caused Ky to lose his prime position as Premier to General Nguyen Van Thieu, who was chosen over Ky as candidate by the military leaders. Ky ran for office as vice-president. Although the Thieu/Ky ticket received only slightly more than one-third of the votes cast, it received a simple majority and took office. Thieu remained in that office until the final days of the war when he resigned and turned over the Presidency to Tanh Van Huong, who in 1971 had replaced Ky as Vice-President.

Return to Pacification

The buildup of U. S. tactical forces began in 1965 and by the end of the year there were 184,000 American troops in South Viet Nam. Another significant event of that year was the formation of the Ministry of Rural Development (MORD), sometimes called the Ministry of Revolutionary Development in English. This ministry, which controlled a growing force of

cadremen working at the hamlet level, became the focal point for civil counterinsurgency within the Vietnamese government for the next three years. Through this ministry USOM's Office of Rural Affairs found a suitable counterpart for its counterinsurgency and technical project activities until 1968 when MORD was succeeded by the Central Pacification and Development Council as the chief coordinating mechanism for pacification (counterinsurgency).

In 1966 the USOM (redesignated USAID in that year) joined with MORD to produce a specific plan aimed at improving the delivery of government services at the local levels and of expanding administrative, agricultural, educational, public health and other public institutions particularly at the hamlet level but also with some projects at the province level. The program was hampered by its newness and the inexperience of the thousands of cadremen who had been recruited to serve as catalysts at the hamlet level. The Viet Cong, by now in full swing against government pacification programs, provided another major hindrance, killing and harassing cadremen and destroying pacification projects. While the program deliberately focused on the hamlet level, most hamlets of Viet Nam were left untouched since available forces could be mustered to work in only a small percentage of the nation's hamlets at any one time.

The Zenith of the U. S. Effort: 1967 - 1972

The year 1967 was one of transition for USAID, moving from a direct role in counterinsurgency in rural areas to one somewhat more in line with traditional policies and practices of economic development. USAID had entered the field of counterinsurgency heavily in 1962 and reestablished its staff of province field advisors late in that year. By 1966, USAID had agricultural, community development and public safety advisors at the region and province level and was dispersing officers at the district level as well. Gradually, a desire to consolidate management of civil and military advisors developed within the U. S. Mission and in Washington.

U. S. Mission Restructured

In November, 1966, the first stage toward consolidating field management was taken. Civilian advisors from all agencies, e.g. A.I.D., USIS, OSA, serving at regional and provincial levels were assigned to a new organization, the Office of Civil Operations (OCO) under Deputy Ambassador William Porter. This move left field operations with only two chains of command, that of the civilian advisors under Ambassador Porter, and that of the military advisors under Gen. William Westmoreland, Commanding General of the Military Assistance Command, Viet Nam (MACV). In May, 1967, a second reorganization placed all field advisors, civil and military, under command of General Westmoreland (See Organizational Chart, Attachment 6). An official carrying the personal rank of Ambassador was placed in charge of these operations. This position was first filled by Ambassador Robert Komer, who reported to General Westmoreland. This combined civil-military

51

organization was designated Civil Operations Revolutionary Development Support (CORDS) and all American activities concerned with counterinsurgency were placed under it. This move provided the U.S. counterinsurgency effort with a single managerial chain which was considered more efficient than multiple chains.

There were 1,977 A.I.D. direct hire employees in Viet Nam on June 30, 1968. Of that total, 1,076 employees were assigned to CORDS. In addition, there were several hundred A.I.D.-financed American employees who were also detailed or assigned to CORDS. (See USAID Personnel Chart, Attachment 7). Although USAID provided the bulk of CORDS civilian personnel, USAID was relieved of direct responsibilities in the counterinsurgency program.

Of USAID's four major goals in 1967, two remained under its primary management responsibility: National Development and Economic Stabilization. The remaining two, Pacification, and War Support and Relief, were placed under the direction of CORDS. Some idea of the balance among the programs can be gained by examining the expenditure of USAID funds directly in these four areas for FY 1968:

	(Million)
Economic Stabilization	\$165.7
War Support & Relief	50.0
Pacification	57.5
National Development	73.5

(Attachment 8 shows distribution of project program dollars by purpose.)

A little noticed activity in 1967 was the small scale trial of a new high-yielding rice, IR 8, which had been developed in the Philippines at the International Rice Research Institute (IRRI). This variety and others developed later at IRRI would become a chief ingredient in Viet Nam's rice production increases in the 1975

USAID also provided technical assistance to the GVN in preparing for local elections by secret ballot in 1967. The renewed GVN interest in representative government at the village level of government was a significant reversal of an entrenched policy: to deny election of local representatives in favor of appointed officials. Elections were held in 1,300 of Viet Nam's 2,000 villages and in 5,000 of its 10,000 hamlets. Presidential and National Assembly elections were conducted this same year.

#### The 1968 Communist Offensive

While the GVN conducted its elections in 1967, the Viet Cong were preparing a major series of attacks on Viet Nam's cities, the Tet offensive of 1968. On the night of January 31, 1968, the City of Saigon and more than 30 Vietnamese province and district towns were attacked on a scale never before mounted by the Viet Cong. The fighting lasted for several weeks and was followed in May by another, lesser offensive. More than 12 thousand civilians were killed, 20,000 wounded and almost a million refugees or displaced persons were generated. Property damage was estimated at 173 million dollars. The effect of these attacks was momentarily to paralyze programs in which USAID had major interests and to set the economy back in several important

aspects.

Immediately after the offensive began, President Nguyen Van Thieu created, on February 2, the Central Recovery Committee which combined the talents of various government ministries to deal with the civil crisis created by the offensive. The committee was charged with directing activities aimed at easing distress of the refugees, restoring facilities in the provincial towns and Saigon, reopening lines of transportation and developing a national spirit of unity to ease the recovery from the attacks. USAID provided food, construction materials, clothing and piaster funds to support the care and resettlement of refugees. It assisted the GVN in dealing with economic problems created by the offensive and by a 30 percent increase in Vietnamese military personnel occasioned by the nationwide mobilization.

Despite the severity of the Viet Cong offensive, the effects on the Vietnamese economy were not as serious as they might have been and by the last half of the year the nation was already regaining economic momentum. USAID's primary interests were in providing resources which enabled the economy to stand up under the economic stresses of war; to foster economic growth in spite of the Tet Offensive; and to assist in long range planning for the hoped-for years of peace to come.

The U. S. military buildup reached its peak in 1969. From an average of 650 / military personnel during the 1954-60 period, it climbed to 542,000 from all branches on January 31, 1969.

Vietnamization and a Decline of Violence

The period 1969-71 marked the start of the Vietnamization Program proclaimed at the Midway Conference in June 1969. Vietnamization involved the gradual turning over to the Vietnamese of military and civilian activities formerly carried out by the Americans. The U.S. pledged to continue military and economic support while the Vietnamese took over the actual fighting and those assistance programs that they wished to maintain.

The Vietnamization program was reflected in USAID's personnel figures immediately. From its peak strength of 1,977 direct hire personnel and 371 on loan from other agencies on June 30, 1968, the numbers dropped to 1,846 and 307 the following year and to 651 and 83 by 1973, several months after the cease-fire. U.S. Project Assistance declined sharply in line with the personnel reductions. From an average of \$256 million annually during fiscal years 1966-68, Project Aid fell to an average of \$139 million during 1969-71. The decline in Project Aid was entirely responsible for a drop in overall economic assistance of the same magnitude during this period.

U.S. Economic Assistance, 1966-71  
(\$Millions\* - Annual Averages)

	<u>1966-68</u>	<u>1969-71</u>
Commercial Import Program	239.8	216.5
Food for Peace	118.4	132.7
Project Assistance	<u>255.6</u>	<u>139.4</u>
Totals	613.8	488.6

The period also saw a marked decline in the level of violence, providing a favorable climate for USAID's overall economic assistance objectives. The return of many refugees to their homes had a beneficial effect on agricultural output. Also aiding in the growth of agriculture was the progressive introduction of miracle rice varieties begun in 1967. The new varieties generally produced twice as much paddy per hectare as local varieties. By 1971, 2,650,000 hectares, some 42 percent of the total cultivated, had been sown to miracle rice varieties. Rice production, which was 4.3 million metric tons in the 1966-67 crop year, rose to 6.1 million tons in 1971-72, an increase of some 42 percent.

A sweeping economic reform program, involving extensive revision of the interest rate, exchange rate, and tariff structures, was carried out with American technical advice during 1970-71. The inflation rate was brought down to 15 percent in 1971 and the investment climate was vastly improved with the elimination of many forms of economic control and the restoration of market incentives.

Through funding and the provision of civil specialists to MACV/CORDS, USAID participated in the reestablishment of the long dormant Village Self-Development Program in 1969. The shift from hamlet to village government represented a major shift of policy in the pacification field. It also placed the national government in direct contact with many citizens for the first time. USAID funding provided a million piasters for each village participating in the restoration effort and, by the time that USAID funding terminated in 1974, most of South Viet Nam's 2,100 villages were participating in the Village Self-Development Program. These 2,100

56'

village governments proved much more capable and manageable than the 10,000 hamlet governments which had received attention in the earlier years of the counterinsurgency effort.

After years of complex technical assistance and negotiating between USAID and GVN, on March 26, 1970, President Thieu launched the USAID-backed Land-to-the-Tiller program which, in many respects, proved to be one of the most dramatic and successful land reform programs ever conducted in the less developed world. During the next three years, more than a million hectares of land were distributed free to the tenants. A portion of CIP counterpart funds were earmarked to assist the Government in compensating landlords. Advisory assistance in execution of the program was also provided.

The period 1969-71 represented a high point in the USAID program in South Viet Nam. Much of USAID's effort had been aimed at stabilization, rather than development, on grounds that this was a prerequisite to economic growth. Economic stabilization appeared to be within reach as the year closed and USAID looked forward to increasing sound investments for economic growth in the ensuing years. Total economic assistance since 1954 reached almost \$4.3 billion by the end of this period.

#### A Decade of Change

There were a number of pluses in the economic development area, as reflected in the changes which had taken place during the decade ending in 1971.

The population had increased by 27 percent--from 14.4 million at the end of 1961 to 18.3 million at the end of 1971. Rice production increased during that period from 4.6 million tons in 1962 to 6.1 million metric

tons in 1971, an increase of 33 percent. Viet Nam exported 85,000 tons of rice in 1962. During the worst of this war decade, it imported as much as 750,000 tons to make up for lost production. But by 1971, imports were down to 160,000 tons.

The Government of Viet Nam supported an army of 400,000 at the beginning of the 1960s. At the close, troop strength was approaching 1.1 million. This expansion, plus other increased activities connected with the prosecution of the war, brought on inflation which began during 1961-64, greatly worsened in 1965 and was brought under control in late 1970 and 1971.

The Viet Cong guerrilla war, which had reached an unacceptable level of violence during the early 1960s had been receding since 1969, when the Vietnamese government began an intensified effort to separate the Viet Cong from the population through pacification. This development represented a reverse in the long term trend and suggested that more time and effort could be devoted to development if the level of violence continued to drop.

A.I.D. formed five major objectives for 1971: 1. Prevent run-away inflation and severe economic dislocations. 2. Ease the suffering of civilians displaced or injured by the war. 3. Assist the Government of South Viet Nam to expand its protection and influence over more of the population, especially in the rural areas. 4. Assist in economic development to the extent possible and feasible under the constraints of wartime conditions. 5. Help the Government of South Viet Nam improve its present range of social and economic services and prepare a basis for planning its future development.

But as the Viet Cong movement seemed on the wane in 1971, the North Vietnamese Army was readying a large-scale invasion which would tip the level of violence upwards once again.

The 1972 Communist offensive differed in two major respects from

the 1968 offensive. First, it did not come as such a surprise to allied forces. Second, it was primarily a conventional military offensive by the North Vietnamese Army rather than a Viet Cong guerrilla action.

Allied intelligence recorded the North Vietnamese buildup early in 1972. There was no doubt the North Vietnamese would attack. The major remaining questions were where and when. This doubt was dispelled when, at the end of March, at Easter, the North Vietnamese Army (NVA) launched a series of major attacks. They moved south from North Viet Nam across the 17th parallel into Quang Tri, the northernmost province of South Viet Nam. They moved east from Laos into Kontum Province and east from Cambodia into Binh Long Province. The fighting raged in varying degrees through the first half of the year. After initially losing control in Quang Tri, the Vietnamese Army, supported by the U. S. Air Force, stabilized the military situation and took back the capital city of Quang Tri as well as part of the province. The North Vietnamese drive at Kontum Province was aimed at capturing the province capital of Kontum, a scenic, tree shaded town nestled in a valley. Although North Vietnamese tanks broke through defenses and entered the city in May, they were driven back. The NVA did not take the city, but remained in control of much of the province. Binh Long's capital of An Loc was the scene of the third bitter battle of this invasion. The NVA did not take this city either but it was leveled during the prolonged siege. Much of the province remained in enemy hands and later served as a headquarters for the Viet Nam Provisional Revolutionary Government.

59

Although the 1972 North Vietnamese invasion was more limited geographically than the Viet Cong Offensive of 1968, it was more damaging in some respects. Another major refugee movement was precipitated, generating 1.2 million refugees, mostly in the Da Nang area of Military Region 1. The invasion was at least partly responsible for the business recession that began in 1972 and for an increase in the inflation rate, from the low 15 percent rate achieved in 1971 to 25 percent in 1972.

On the plus side, the refugees were cared for with more dispatch than in the past. Exports, still small, doubled over 1971. Tax collections increased. The land reform program moved forward largely unimpeded by the invasion.

#### The Cease-Fire and Its Aftermath, 1973-1975

Rumors of an impending cease-fire which began in late 1972 were followed with an announcement on January 23, 1973 by President Richard Nixon that a cease-fire would begin on January 28, 1973. On that day, at 8 a. m., Saigon time, the ships in the Saigon River sounded their whistles. They were joined by church bells for several minutes as the cease-fire began. But within 24 hours there were charges and counter-charges of violations by both sides. The level of violence remained high in 1973, despite the cease-fire.

The cease-fire did, at least, bring an end to U. S. military participation in South Viet Nam. Indeed the military effort had been phasing out since 1969 but the remaining advisory and tactical personnel were removed under the terms of the agreement. Left behind were a few U. S. marines guarding Embassy buildings and a handful of military

personnel in the Defense Attache Office. The DOD, at the same time, recruited several thousand American civilians to aid in maintaining certain physical structures until they could be turned over to the GVN and to provide technical assistance to the Vietnamese armed forces.

For more than ten years, USAID's program considerations had been largely dominated by the exigencies of the war. Much of its funds and many of its personnel had been committed to programs connected with counterinsurgency, rather than those which related primarily to economic development. Hence, the annual planning factors for USAID programs involved a heavy input of both political and military considerations. From the cease-fire of 1973 forward, USAID, based on the prospects of eventual effectiveness of the cease-fire and despite the continuing violence, concluded that its programs should be greatly narrowed and pointed more directly at economic self-sufficiency for South Viet Nam. For that reason, programming was thenceforth dependent more on the economic than on the military situation.

#### Status of the Vietnamese Economy

The principal factors in the economic situation in the wake of the cease-fire were the impact on employment resulting from the U. S. force withdrawal and the precipitous decline in real external assistance. The latter was a result both of the loss of dollar earnings associated with the U. S. troop presence and the rapid rise in import prices during 1972-74. The withdrawal of U. S. troops thus marked the start of a painful economic transition. By the end of 1974 the government was still struggling to employ productively the substantial human and material resources that had

been idled by the U. S. pullout, and to move the economy onto the path of self-sustaining growth. Next to the continuing war itself, the economy represented the most difficult challenge facing the government.

An inventories buildup, in part related to the withdrawal and declining purchasing power, took place in the first quarter of 1972. The Easter offensive, launched on April 1, 1972, precipitated the economic downturn, which appeared in store anyway, and forced postponement of plans for finally turning from pursuit of the war to economic development. Piaster purchases by the U. S. sector fell from the peak figure of \$403 million in 1971 to \$213 million in 1972. All forms of import support -- defined as CIP, Food For Peace, and piaster purchases -- declined from \$872 million to \$596 million in the same period. Compounding the problem for Viet Nam, import prices in mid-1972 began a remarkable upsurge which brought a doubling of the import price level. Accompanying the surge in import prices were severe shortages of critical materials and commodities on the international market (synthetics, iron and steel, fertilizer, cement) that aggravated the problems of the business community. The final calamity in 1972 was bad weather which damaged the 1972-73 rice crop, causing a 5 percent decline in output from the previous year.

By 1973 the gap left by the U. S. pullout became the dominant fact in the economy. U. S. sector piaster purchases fell to \$96 million, which was to be the approximate residual rate. The number of Vietnamese directly employed by the U. S. sector fell to 17,273 by September 30, 1973, compared with a peak employment of 160,041 in June 1969. It was estimated that the number employed indirectly by the U. S. sector dropped

62

by at least as much. Although exports did well, rising from \$23 million in 1972 to \$60 million in 1973, for the most part the new investments needed to provide employment for those displaced did not take place. The war itself was the inhibiting factor. Worldwide inflation continued throughout the year. Imports were up six percent in nominal terms, but down 22 percent in real terms. Along with recession and rising unemployment, Viet Nam experienced its worst price inflation ever; consumer prices in Saigon rose by 62.5 percent during 1973.

The first quarter of 1974 saw a continuation of the rapid rate of inflation that had prevailed over the past two years. In fact, the rate of inflation during the quarter accelerated somewhat under the impact of sharply higher petroleum prices. In the second and third quarters, however, the rate of price increases slowed considerably, to an annual rate of about 10 percent. U. S. import support rose in FY 1974 -- to \$693 million from \$540 million in FY 1973. CIP assistance increased from \$226 million to \$285 million and was augmented by a \$50 million Program loan that was administered through the CIP mechanism. However, rising prices again meant a reduction in import support measured in real terms. Imports in 1974 reached a record high of \$887 million, but in real terms were 19 percent below 1973. The recession continued throughout the year and urban unemployment continued to mount. By the end of 1974 unemployment was estimated at 15 to 20 percent of the labor force.

Progress was made in a number of areas during 1973-74 notwithstanding the general recession. The agricultural sector did relatively well. The rice harvest rose from 5.9 million tons in 1972 to 6.6 million tons in 1973

and 7.1 million tons in 1974. By the end of 1974 the country was finally producing enough rice to meet its own needs. It was felt that if further production gains could be managed in 1975 and beyond, the country could enter the export lists in rice and add substantially to its foreign exchange earnings.

A major event was the completion of the Land-to-the-Tiller Program in March, 1973 under which 800,000 hectares of farm land were distributed to some four million former tenants.

Exports continued to rise impressively through the first quarter of 1974, then leveled off under the impact of declining markets abroad for Viet Nam's principal export products -- frozen shrimp, rubber, and pine logs. Export earnings in 1974 totaled \$75 million.

Tax collections, spurred by a major shakeup of the Tax Directorate in 1972 and a number of new tax measures, rose dramatically in 1972 and 1973 before leveling off -- finally -- in response to the business recession. Domestic tax revenues rose by 47 percent in 1972 and another 93 percent in 1973. The two-year increase of 183 percent far exceeded the consumer price increase of 107 percent during the same period; thus, the increase was a real one. U. S. advisors played a key role in the restructuring of the tax system during this time.

Private foreign investment interest was minimal during 1972-74. However, the discovery of traces of oil by foreign companies drilling off Viet Nam's West coast during 1973 raised excited hopes of eventual commercial development. Foreign oil companies paid \$47 million to the GVN for oil exploration rights during 1973-74. Official third country aid was mostly

in the area of project assistance, but balance of payments loans were received from France, Japan, and Taiwan. Imports financed by such loans first took place in 1974, reaching \$26 million.

Taking 1972-74 as a whole, U. S. import support declined by 65 percent and imports by 46 percent, in real terms. Industrial production declined by about 40 percent. Agricultural production increased at a rate at least equal to the 2.6 percent rate of population growth. Thus, the burden of the recession fell almost entirely on the urban areas and the 40 percent of the population living in the cities. For the economy as a whole, per capita income is estimated to have declined during this period by 15 to 20 percent.

Policy Shifts to Accommodate Cease-Fire and Declining Aid Levels

The cease-fire created an awkward planning problem for both the GVN and USAID. Should planning be done on the assumption that the fighting would continue, that it would decrease gradually or that it would stop altogether?

The decision was made to assume that the level of violence would be no greater than it was in 1972 and that it would diminish gradually in several years to manageable proportions. Maintenance of bearable economic conditions and progress toward self-sufficiency, were judged to be important during this period if GVN were to maintain the allegiance of its people while fending off continued attacks by its enemies.

From 1973 through the final months of the war in 1975, USAID concentrated on two major objectives: continued humanitarian assistance to refugees and other persons uprooted by the war; second, assistance to the

GVN in moving from a state of external dependence to one of economic self-sufficiency. The first objective was aided by the earmarking of dollars for humanitarian assistance under the so-called "Kennedy Amendment." Direct dollars obligated under the Kennedy Amendment totaled \$88 million during FY's 1972-75. The dollars, which, unlike CIP funding, were available to the GVN for imports without restriction as to source, supported GVN programs in the areas of refugee relief and resettlement, and child care. USAID's Relief and Reconstruction Division was the largest in terms of personnel employed during most of this period.

The effort to move the economy toward self-sufficiency faced a dilemma at the outset; namely, an effort that, by any economic reasoning, should require large amounts of capital input would have to take place during a period of declining real aid. Yet there was nothing to do but meet the problem head-on. Indeed, precisely because aid levels were not likely to rise significantly -- if at all -- in the future, the drive for self-sufficiency assumed a special urgency.

The GVN, with the aid of U. S. technical advice and support, took a number of important practical steps toward development during 1971-74. Foremost of these were the economic reforms of 1970-71 which established a realistic exchange rate of structure and paved the way for a revival of exports. The Foreign Investment Law was rewritten in 1971. The Industrial Development Center was converted to a full-fledged Development Bank, also in 1971. The National Economic Development Fund was established on March 28, 1972 with 10 billion piasters of capital provided from U. S. counterpart.

A largely moribund private lending institution called Societe de Financiere et de Development (SOFIDIV) was converted to an active private investment bank, renamed Investment and Development Bank (IDEBANK) in 1973. An Investment Service Center and an Export Promotion Center were started in 1972. Finally, the GVN Ministry of Planning, upgraded from Commissariat General status in June 1971, produced a Four-Year Plan for 1972-75. The planners had the bad luck to be overtaken by events, since the Easter offensive of 1972 upset their calculations from the start, but the Plan was rated a creditable effort in terms of internal consistency and logic.

These were all useful steps and they produced results in terms of development loans and sharply rising exports, the recession notwithstanding. By 1974, however, the Mission felt the need for a Plan that would demonstrate to the Congress that there could be an end to large-scale aid to Viet Nam.

#### The Five-Year Plan for Self-Sufficiency

The Five-Year Plan for economic self-sufficiency, which formed the basis for the funding level requested from the Congress in FY 1975, was predicated on the notion that if the U.S. would supply relatively large levels of aid during an initial period, it would be possible to phase out U.S. concessional aid in five years. The "adequate" initial aid level was proposed at \$750 million in FY 1975. The plan postulated a five percent rate of economic growth based on rapidly rising investment and a highly favorable capital:output ratio (i.e. the amount of output that can be had from a given volume of investment). USAID economists were fairly certain that given South Viet Nam's large pool of underemployed resources, the assumptions in this area were not unduly optimistic. Some of the other

67

assumptions underlying the plan were more questionable. There would have to be a gradual winding down of the war. Exports would have to rise very rapidly. Most important, aid and investment from third countries and international institutions would have to rise quite rapidly. Indeed, the securing of additional third country aid became so important during this period as almost to constitute a separate USAID objective in itself-- along with humanitarian aid and the goal of self-sufficiency.

AID planners had difficulty defending the plan against critics who objected that one or another of the plan goals was unrealistic. It was not easy to make the case that not all goals had to be met for the overall plan to make sense. At any rate the plan was not overwhelmingly endorsed by the Congress, which was unable to agree on an economic aid bill before the Christmas recess. By the time a bill finally was acted upon in December 1974, the question of economic aid to South Viet Nam had become mixed up with the deterioration in the overall situation and the appropriation in March 1975 for FY 1975 was the lowest since 1964, even in nominal terms: \$245 million.

Military aid for South Viet Nam had been fixed at \$700 million in FY 1975. Within this budget, the Department of Defense was not able to replace major war equipment, tanks, planes and trucks, on a one-to-one basis, as allowed under the cease-fire agreements. It restricted its spending to supplying critical consumable items such as ammunition and fuel. While the GVN was appealing for supplemental U.S. military and economic assistance in late 1974 and early 1975, the pace of fighting rapidly accelerated. Communist forces, although still much smaller than

68

South Viet Nam's 1.1 million army, had been built up in numbers since the 1972 invasion. Further, unlike the South Vietnamese Army, the communist forces were not tied down by defense of population areas and physical infrastructure, and they were well supplied with tanks and artillery weapons which had not been used by them during earlier insurgency stages of the war.

In February 1975, the communists captured and permanently held the first of South Viet Nam's province capitals, Phuoc Binh in Phuoc Long province. This precipitated the first refugees of this final campaign. On March 14, 1975, President Thieu, faced with mounting North Vietnamese pressure in the Central Highlands and declining aid from the outside, announced to his generals his decision to withdraw temporarily from Darlac, Pleiku and Kontum in the Central Highlands. But the withdrawal turned into a disorderly retreat, which precipitated a second retreat in I Corps beginning at the ancient Imperial Capital of Hue. Thousands of refugees streamed into Da Nang. When it became clear that northern I Corps was collapsing, air and sea evacuation was launched to southern coastal centers which were considered safer at the time, e.g. Nha Trang, Cam Ranh, Ninh Thuan, Binh Thuan and Vung Tau. But the course of events moved too swiftly and, by early April, it was apparent that these areas also would fall. A last ditch effort was made to resettle refugees in the Delta and some ships laden with evacuees headed for Phu Quoc island off the coast of Kien Giang. Some 40,000 had reached there by the time Saigon fell.

On April 10, President Ford made a last attempt to gain aid for the South Vietnamese Army, which was making a stand in the III Corps area

65

surrounding Saigon. But within a few days, GVN forces had been reduced to five divisions surrounded by 16 to 20 North Vietnamese divisions, as the rest of the North Vietnamese Army crossed into South Viet Nam for the ultimate occupation. President Thieu resigned on April 21, and President Ford announced on April 24 that the war in Viet Nam was over for the United States.

The U.S. speeded up the evacuation of its employees and citizens, which had been underway for some time and, by early morning April 30, the evacuation was completed, save for some seventy-five Americans remaining behind either voluntarily or in captivity.

As many Vietnamese were evacuated as could be accommodated during the last hectic days. Approximately 140,000 managed to leave, all but 6,629 of whom eventually made their way to the U.S. Processing centers were quickly established in the Philippines and Guam to handle the refugees and camps were set up in the U.S. at Camp Pendleton, California; Fort Chaffee, Arkansas; Camp Eglin, Florida and Indiantown Gap, Pennsylvania. As of December 21, 1975, all of these camps had been closed and the refugees are now settled in towns and cities all over the country once again to start a new and, hopefully, more settled life.

## POSTSCRIPT

The residual value of the U.S. economic assistance programs in South Viet Nam is obscured by the central fact that the form of government, which was supported by the United States for twenty-one years, was overthrown in 1975. Thus, in purely political terms, one would conclude that these programs, taken together, were not successful, if their overall purpose was to sustain the Government of South Viet Nam. But this is far too simplistic. Economic assistance is just one of several foreign policy tools applied to the achievement of U.S. interests and, because of the interplay among political, military, diplomatic and economic factors, it is very difficult to isolate any one tool or factor from the others as a determinant in and of itself. Furthermore, even if one agrees that maintenance of the GVN was the primary goal of economic assistance, there were many beneficial spinoffs for the people, as described in Volume II of this report, in such areas as development of trained manpower in a wide range of skills; institutional development in many spheres of public and private life; technological and scientific advances, particularly in agriculture and industry; and physical infrastructure in virtually all walks of life.

Nowhere can this point be better illustrated than with rice--the symbol of security and prosperity. With the introduction of the new "miracle" varieties of seed, proper application of fertilizer and insecticides, and improved overall farming practices, rice production reached new records, despite the fact that the war deprived the South Vietnamese access to large segments of formerly productive land.

-71-

The farmers of South Viet Nam, once too poor to pay taxes, came into their own in the late 1960s. They bought their own tractors and in a few years were able to pay their own taxes to support those government services which were of most importance to them.

The concept of government itself was greatly altered during the years of U.S. involvement. Local governments, once neutralized by the desire of the Vietnamese chief executive to exercise strong central control over the people, developed into locally elected bodies with greatly expanded powers to make decisions without consulting the central government.

Viet Nam's education<sup>al</sup> system, with American advice and assistance, developed far beyond any goal which might normally be expected in a country with such limited assets and such huge military commitments. In 1975, mass education for all was far closer to reality in South Viet Nam than in its neighboring countries.

The road system in South Viet Nam, despite its selection as a chief target by the Viet Cong, grew to surpass most comparable developing countries and provided a nationwide network on which to move goods and people.

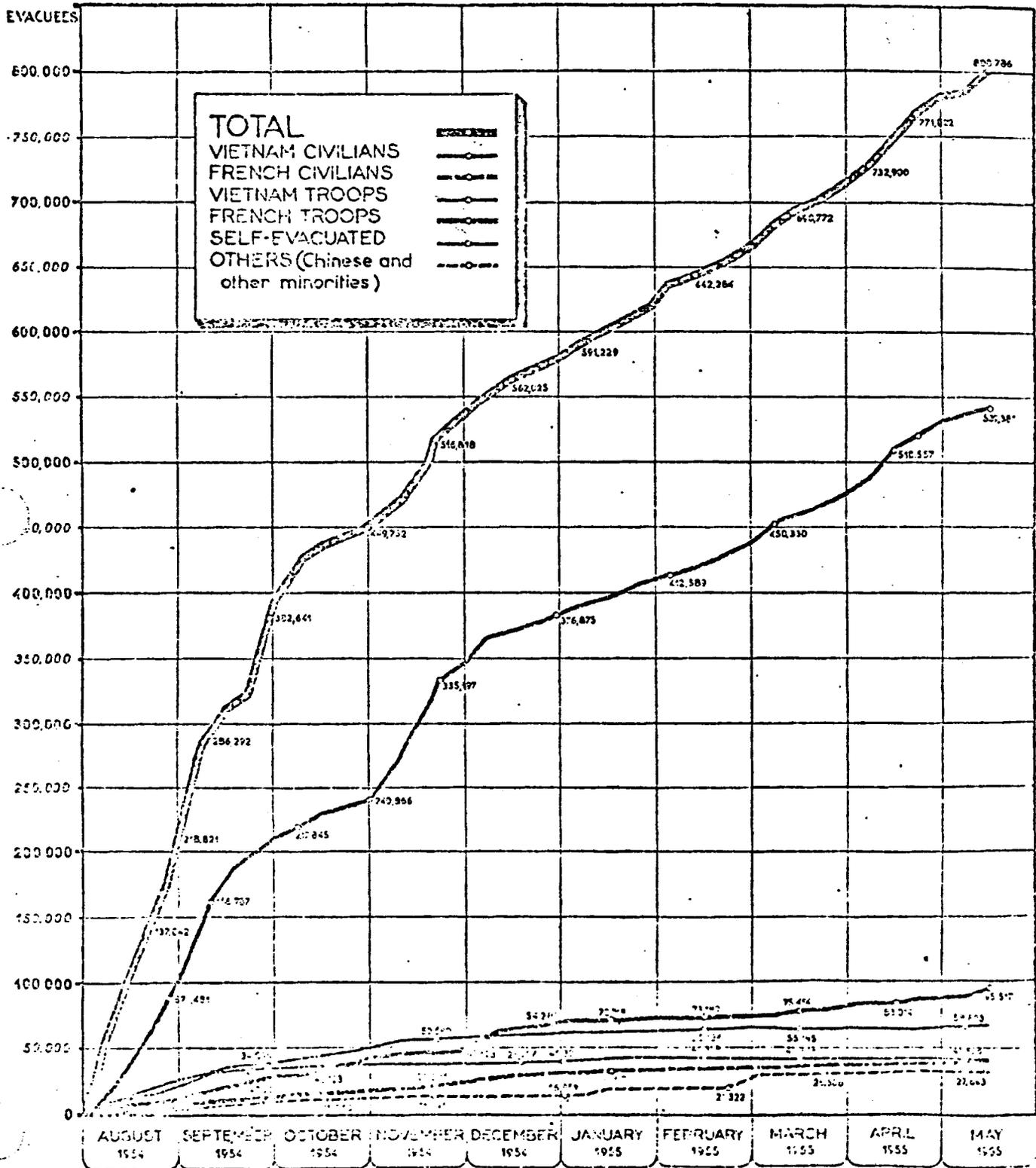
Through the years, tens of thousands of South Vietnamese were trained within the country or abroad in virtually every professional, technical and administrative field--doctors, engineers, educators, accountants, managers, public administrators, etc. This large and valuable resource, for the most part, remains in South Viet Nam today.

The question might arise whether these human and material assets will be used under another government. It seems logical to assume that the

ability to grow more rice, to educate more children or to repair a tractor are advantages which any government, no matter what its political bent, would be desirous of continuing. A balanced evaluation of the effects of U.S. economic assistance in South Viet Nam must take into consideration not only the support given the Government of South Viet Nam but the assistance given the people of South Viet Nam as well.

# EVACUATION FROM NORTH-VIETNAM

AUGUST 19, 1954 TO MAY 19, 1955



74

U.S. Economic Assistance to Viet Nam, 1954-75  
(Obligations in \$ Millions)

Year <sup>a/</sup>	(1) CIP <sup>b/</sup>	(2) FFP	(3) Project & Other AID <sup>c/</sup>	(4) Total Aid
1954	-	0.1	-	0.1
1955	253.7	2.2	66.5	322.4
1956	174.7	14.3	21.0	210.0
1957	210.9	22.8	48.5	282.2
1958	151.9	9.6	27.5	189.0
1959	146.4	6.5	54.5	207.4
1960	135.6	11.3	34.9	181.8
1961	111.2	11.5	29.3	152.0
1962	94.1	31.9	30.0	156.0
1963	95.0	52.6	48.3	195.9
1964	113.0	59.1	52.7	224.8
1965	150.0	49.9	75.0	274.9
1966	399.3	143.0	194.2	736.5
1967	160.0	73.7	334.4	568.1
1968	160.1	138.5	238.1	536.7
1969	130.0	99.4	184.1	413.5
1970	238.5	110.8	127.4	476.7
1971	281.0	188.0	106.7	575.7
1972	313.0	67.8	73.8 <sup>d/</sup>	454.6
1973	226.2	186.8	87.2 <sup>d/</sup>	500.2
1974	335.1 <sup>e/</sup>	235.3	48.3 <sup>d/</sup>	618.7
1975	143.2	57.7	45.0	245.9
Totals	4022.9	1572.8	1927.4	7523.1

Notes: (a) Fiscal years for all but piaster purchases, which are on a calendar year basis.

(b) Does not include de-obligations.

(c) Including also Direct Dollar Support from 1972-75. See Note (d)

(d) Broken down as follows:

	Project Aid	Humanitarian Aid (Direct Dollar Support)	Total
FY 72	71.4	2.4	73.8
FY 73	56.2	31.0	87.2
FY 74	22.3	26.0	48.3
FY 75	15.7	29.3	45.0

(e) Includes Program Loan of \$50 million

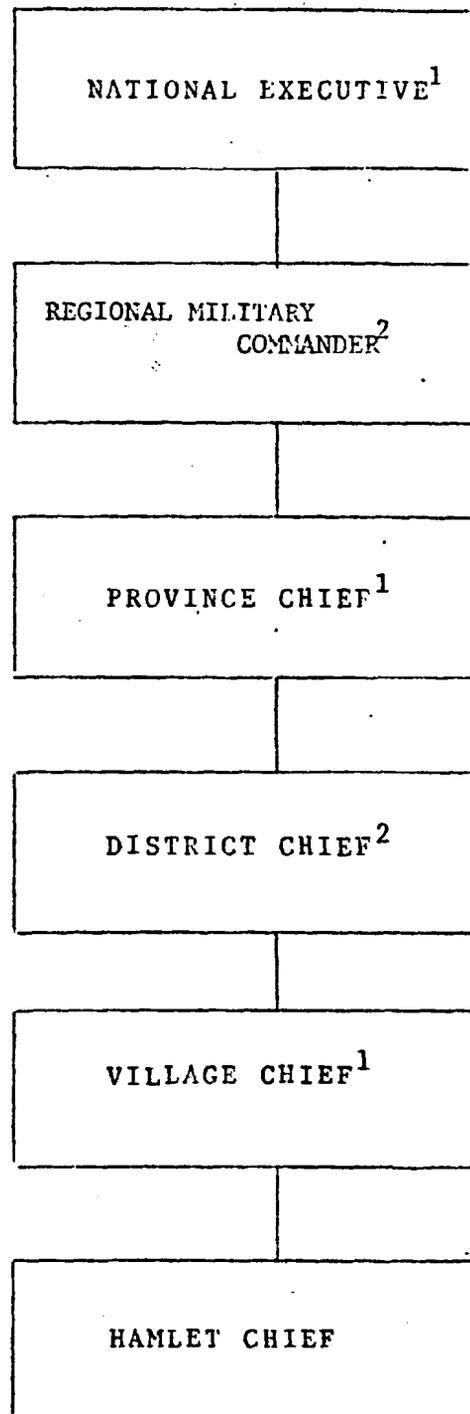
Sources: AID Statistics and Reports Division, "U.S. Overseas Loans and Grants"; Viet Nam Program Summaries, AID.

## SCHEDULE OF JOINT VIETNAMESE-AMERICAN PROJECTS

As of FY 1958

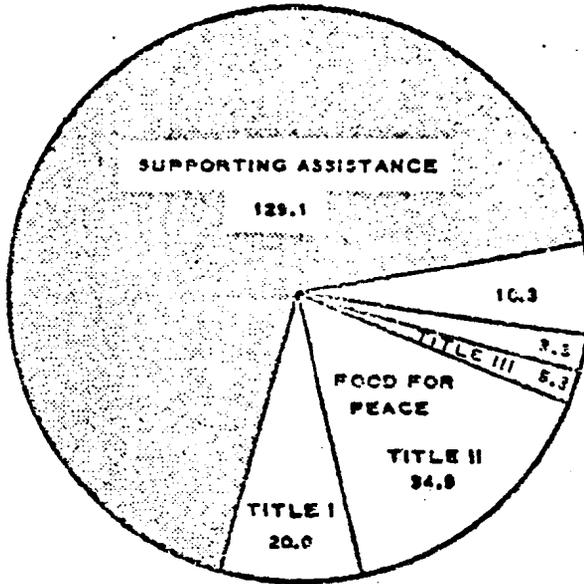
PROJECT TITLE	Fiscal year begun	Estimated completion of aid
<b>AGRICULTURE AND NATURAL RESOURCES</b>		
— Agricultural Extension and Information .....	'55	'61
— National Agricultural College and General Training .....	'54	'60
— Research in Diversified Crops .....	'55	'65
— Small Water Control System .....	'55	'61
— Administration of Agrarian Reform .....	'55	'58
— Land Development (Rural Resettlement) .....	'57	'60
— General Livestock Development .....	'56	'61
— Agricultural Economics and Statistics .....	'57	'64
— Agricultural Production Credit .....	'55	'62
— Agricultural Cooperatives .....	'55	'62
— Development of Marine Fisheries .....	'52	'61
<b>INDUSTRY AND MINING</b>		
— Keng-Son Coal Exploration Survey .....	'57	'58
— Industrial Development Center .....	'57	'64
— General Industrial Survey .....	'57	'58
— Craft Development .....	'57	'62
<b>TRANSPORTATION WORKS</b>		
— Highways and Bridges .....	'55	'63
— Viet-Nam Railways System .....	'57	'62
— Saigon Port Lean .....	'52	'57
— Waterways of Viet-Nam .....	'55	'60
— Dredging the Canals of Viet-Nam .....	'57	'60
— Telecommunications Engineering (Thailand, Viet-Nam and Laos) .....	'55	'65
— Micro-Wave Telecommunications System, South Viet-Nam .....	'66	'65
— Electric Power Development .....	'56	'63
— Rural-Urban Water Supply .....	'56	'60
— Saigon-Cholon Water System Survey .....	'55	'58
— Improvement and Expansion of Aeronautical Ground Facilities .....	'51	'62
<b>HEALTH SERVICES</b>		
— Malaria Eradication Program .....	'55	'63
— Health Services Development .....	'52	'61
— Medical and Allied Education, including Nursing .....	'57	'62
<b>EDUCATION</b>		
— Technical-Vocational Education .....	'55	'64
— Elementary Education .....	'55	'62
— Secondary Education .....	'57	'60
— Teacher Training and Higher Education .....	'53	'64
— Adult Literacy Training .....	'51	'59
— Textbook Development and Special Services .....	'56	'60
<b>PUBLIC ADMINISTRATION</b>		
— Central Supply System .....	'56	'60
— National Institute of Administration and MSU Administrative Support .....	'55	'62
— National Institute of Statistics .....	'56	'63
— Training for Public Administration Participants .....	'56	'65
— Civil Police Administration .....	'56	'61
<b>COMMUNICATIONS</b>		
— Development of Government Information Facilities .....	'51	'61
— National Radio Network .....	'56	'61

ADMINISTRATIVE APPARATUS  
GOVERNMENT OF VIET NAM  
EXECUTIVE BRANCH



1. Levels of government with power of taxation.
2. Levels of government not established by constitution but established ad hoc in order to cope with war-related demands.

FIGURE 4 : TOTAL USOM/VIETNAM OBLIGATIONS - FISCAL YEAR 1963



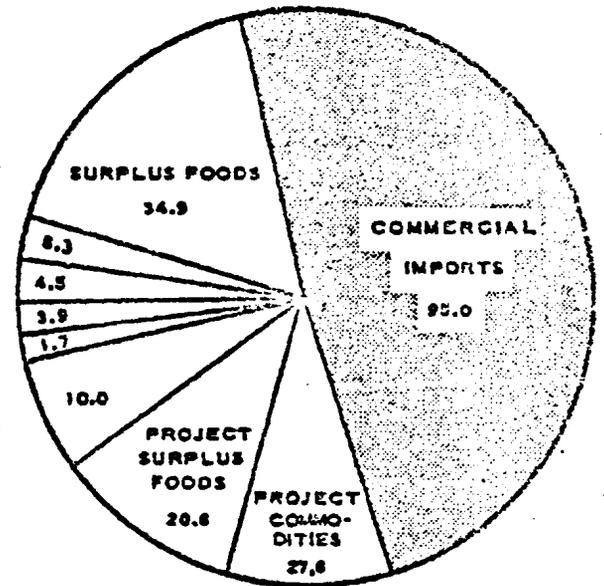
BY CONGRESSIONAL APPROPRIATION

"WHERE IT CAME FROM"

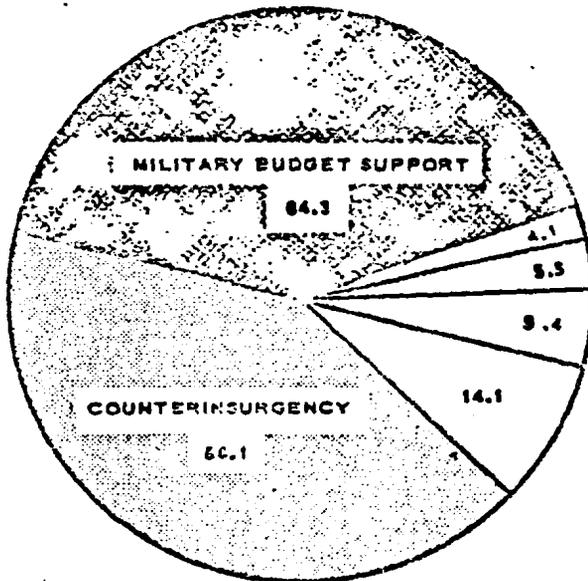
DEVELOPMENT GRANTS  
CONTINGENCY FUND

BY TYPE OF OBLIGATION

"HOW IT WAS TO BE SPENT"



FOOD DISTRIBUTED BY CHARITIES  
DIRECT HIRE PERSONNEL  
CONTRACT SERVICES  
PARTICIPANTS \*  
SPECIAL DIRECT  
PURCHASE OF PIASTERS



TECHNICAL SUPPORT \*\*  
FOOD DISTRIBUTED BY CHARITIES  
ECONOMIC - SOCIAL DEVELOPMENT

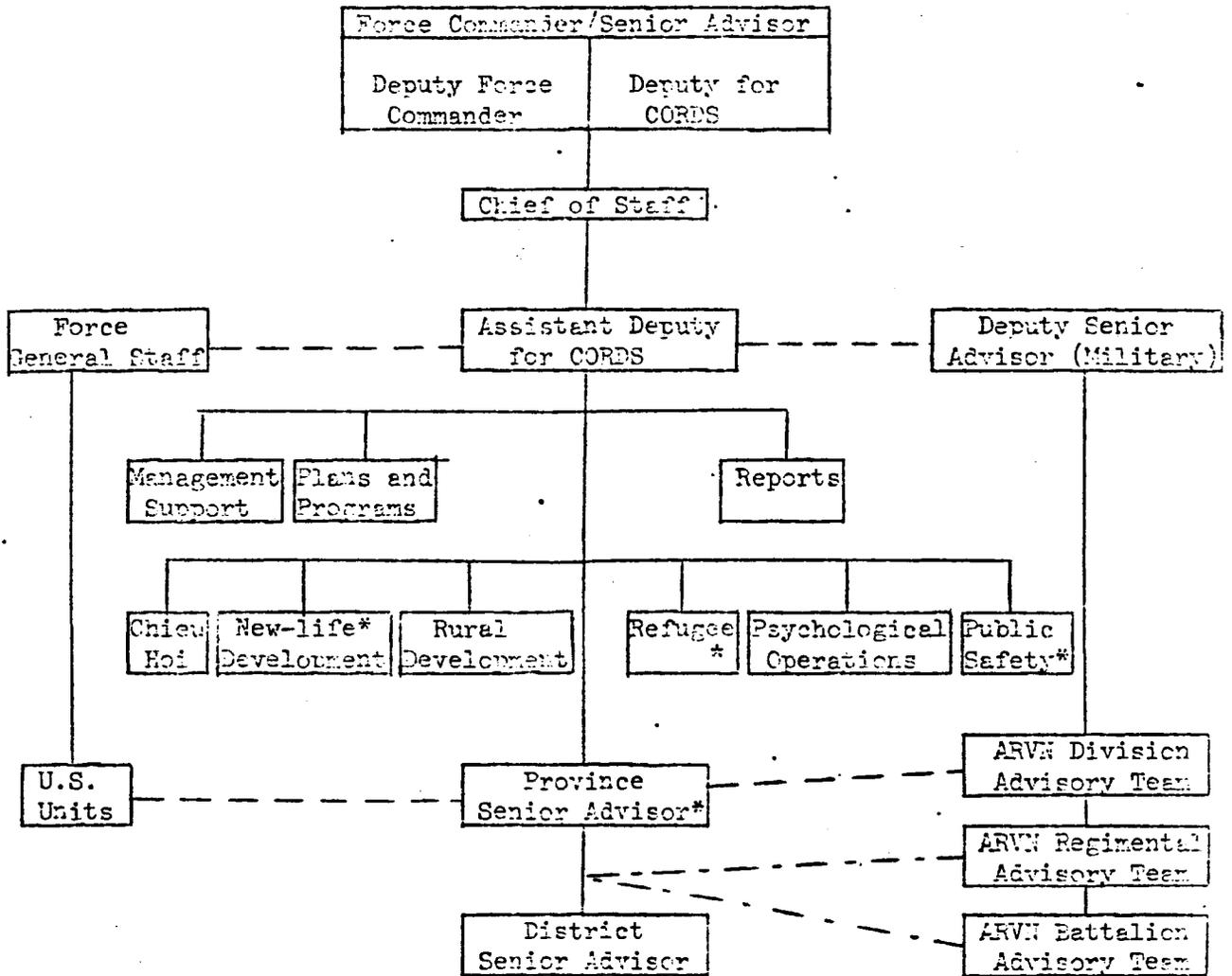
WAR INFRASTRUCTURE

BY PURPOSE  
"WHY IT WAS TO BE SPENT"

\* VIETNAMESE STUDYING ABROAD.

\*\* USOM PROGRAM OPERATION EXPENSES WHICH CANNOT BE ALLOCATED TO ONE SPECIFIC PROGRAM OR PURPOSE.

CORDS Field Organization



----- Coordination--Military and CORDS matters  
 - - - - - Operational Control when units assigned an RD direct support mission

\* These functions formerly conducted under USOM field operations.

USOM, USAID & CORDS  
EMPLOYEES ON BOARD  
(1954-1975)

As of June 30	U.S. Direct Hire *			Foreign Nationals Direct Hire			On Loan From Other Agencies	U.S.	F.N.	TOTALS
	USAID	CORDS	TOTAL	USAID	CORDS	TOTAL				
(Indochina)										
1951	33		33	71		71	8			
1952	62		62	157		157	16			
1953	73		73	191		191	11			
1954	76		76	226		226	13			
(South Viet Nam)										
1955	127		127	453		453	11	1		1
1956	153		153	586		586	8	39		39
1957	159		159	730		730	19	148		148
1958	164		164	657		657	18	342		342
1959	172		172	567		567	20	352		352
1960										49
1961	202		202	603		603	18	171		171
1962	206		208	628		628	15	96		98
1963	289		289	735		735	40	102		102
1964	357		357	864		864	53	166		166
1965	543		543	1086		1086	103	57	275	332
1966	843		843	1144		1144	97	136	380	516
1967	1674		1674	1848		1848	219	264	634	948
(CORDS)**										
1968	901	1076	1977	3118		3118	371	501	2157	2658
1969	762	1084	1846	2690	617	2690	307	787	4708	5495
1970	610	943	1553	2057	192	2057	255	442	2055	2497
1971	554	756	1312	1841	114	1841	194	293	1170	1463
1972	462	557	1019	1436	13	1436	148	224	682	906
1973	429	222	651	1244		1244	83	222	480	702
1974 ***	428		428	973		973	23	168	436	604
1975	344		344	927		927	19	118	401	519

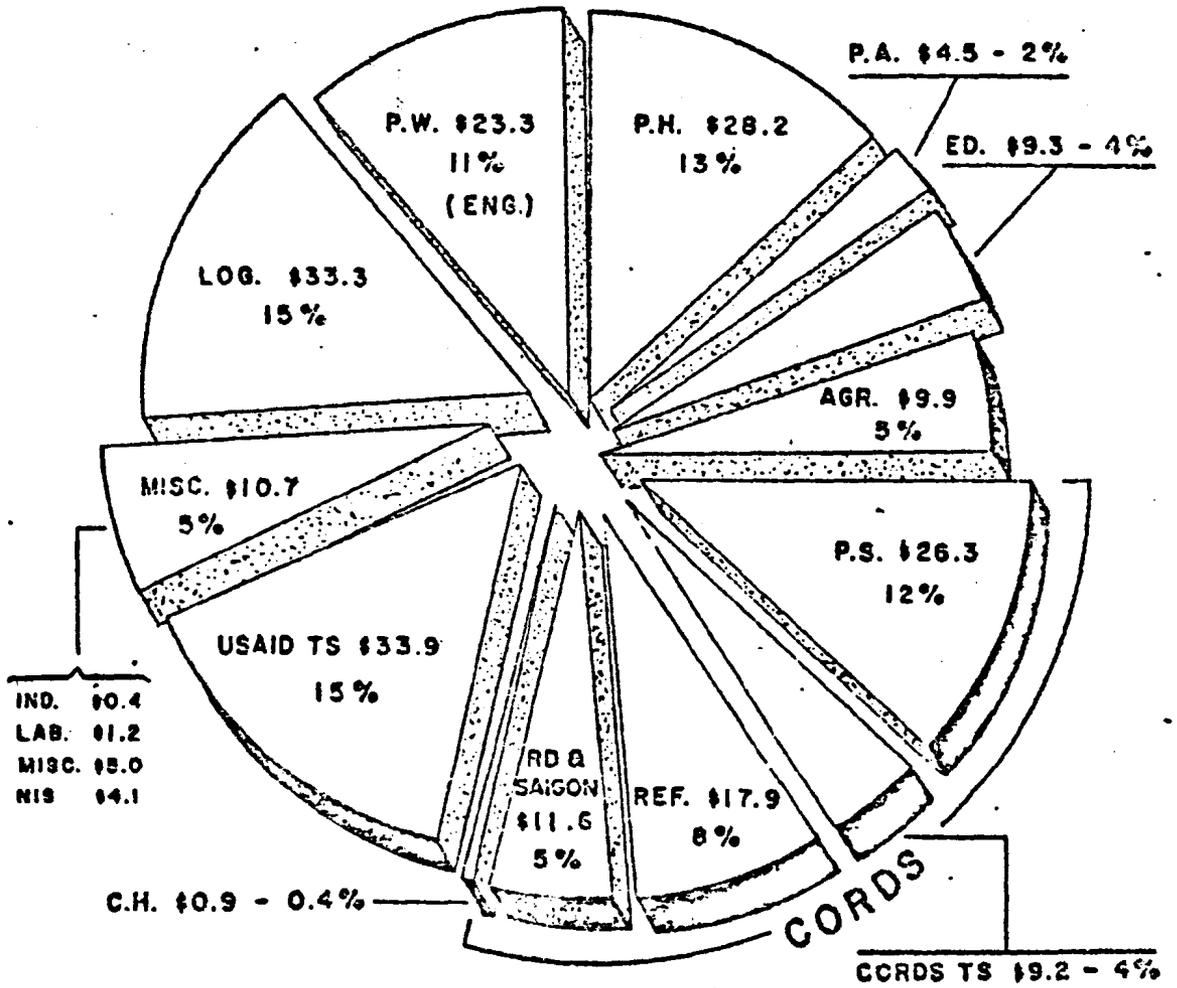
\* U.S. direct hire figures exclude USAID/VN personnel stationed outside VN.

\*\* Foreign National personnel not available for 1968.

SOURCE: A.I.D. Office of Personnel and Manpower

\*\*\*As of March 31, 1975.

# PROJECT PROGRAM DOLLARS FY 1968 ( IN MILLION DOLLARS )



TOTAL : \$219.0

U.S. ARMY AND TOTAL U.S. MILITARY PERSONNEL  
IN SOUTH VIET NAM<sup>1/</sup>

DATE	U.S. ARMY PERSONNEL	TOTAL U.S. MILITARY PERSONNEL
31 Dec 1960	800	900
31 Dec 1961	2,100	3,200
31 Dec 1962	7,900	11,300
31 Dec 1963	10,100	16,300
31 Dec 1964	14,700	23,300
30 Jun 1965	27,300	59,900
31 Dec 1965	116,800	184,300
30 Jun 1966	160,000	267,500
31 Dec 1966	239,400	485,300
30 Jun 1967	285,700	448,800
31 Dec 1967	319,500	485,600
30 Jun 1968	354,300	534,700
31 Dec 1968	359,800	536,100
*31 Jan 1969	365,600	542,400
30 Jun 1969	360,500	538,700
31 Dec 1969	330,300	474,400
30 Jun 1970	297,800	413,900
31 Dec 1970	250,700	335,800
30 Jun 1971		241,683
31 Dec 1971		158,320
30 Jun 1972		48,005
		35,865
31 Dec 1972		24,108
10 Mar 1973		7,047
28 Mar 1973		--

<sup>1/</sup> Logistical Support, Viet Nam Studies, by Lt. Gen. Joseph M. Heiser, Jr. (Department of the Army, Washington, D. C. 1974, pg. 14) 1971-1973; Office of the Army Historian, Washington, D. C.

\* Indicates peak strength in South Viet Nam  
Between 1954-1960 U.S. Military Strength averaged about 650 advisors.

AN ECONOMIC OVERVIEW OF SOUTH VIET NAM

## ECONOMIC OVERVIEW

### OUTLINE

#### FORWARD

- I Introduction; Background to U.S. Involvement
- II The Vietnamese Economy in 1954
- III Early Difficulties and the U.S. Response
- IV 1954-64
- V The Vietnamese Economy in 1964
- VI The Import Economy, 1965-67
- VII The Tet Offensive
- VIII Recovery From The Tet Offensive
- IX End of the Old Ways, January 1969 - August 1970
- X Economic Reform and Progress, September 1970 - March 1972
- XI Misfortune Befalls, 1972
- XII Recession, Declining Aid, and the Struggle For Self-Sufficiency, 1973-74
- XIII The End, 1975
- XIV A Footnote on Corruption
- XV Conclusion

#### TABLES

## TABLE OF CONTENTS

### FORWARD

- I Introduction; Background to U.S. Involvement
- II The Vietnamese Economy in 1954
- III Early Difficulties and the U.S. Response
- IV 1954-64
  - A. Economic Activity
    - 1. 1955-60
    - 2. 1961-64
  - B. Fiscal and Monetary Developments
  - C. Balance of Payments
  - D. U.S. Aid Directions.
  - E. Exchange Rate Developments
    - 1. 1955-61
    - 2. After January 1, 1962
    - 3. Summary; appropriateness of the rate level
  - F. GVN Economic Policies
- V The Vietnamese Economy in 1964
- VI The Import Economy, 1965-67
  - A. Inflationary Pressures, 1965-66
    - 1. U.S. Force Buildup
    - 2. GVN Employment
    - 3. Diversion of Resources From Production
    - 4. The A.I.D. Response
    - 5. Progress of Inflation
      - a. Method of analyzing inflation; the monetary gap
      - b. Inflation, 1964-66
    - 6. Imports, 1965-66; Port Congestion
    - 7. Honolulu Conference, February 1966; Tax Increases
    - 8. The Devaluation of June 1966
    - 9. Effects of the 1966 Devaluation
      - a. On Inflation
      - b. On import licensing
      - c. On foreign exchange reserves
    - 10. MACV Expenditure Control Program
    - 11. Inflation in 1967; The Rice Price

TABLE OF CONTENTS - continued

- B. Production and Incomes, 1965-67
  - 1. Domestic Production
    - a. Rice
    - b. Other agriculture
    - c. Industry
  - 2. Goods Availability
  - 3. National Accounts
  - 4. Income Distribution
  
- C. Imports, 1964-67
  - 1. Volume of Imports
  - 2. Composition of Imports; CIP Program
  - 3. Implications of the Import Program
  
- VII The Tet Offensive
  - A. Economic Impact
  - B. Mobilization and the Budget
  - C. Monetary Gap and Inflation
  - D. Balance of Payments and Exchange Reserves
  
- VIII Recovery From The Tet Offensive
  - A. The Surge in Import Activity
  - B. Agricultural Activity
  
- IX End of the Old Ways; January 1969 - August 1970
  - A. Agricultural Prosperity
  - B. Industry
  - C. Import Licensing and Reserve Drain
  - D. Growing Inflationary Threat
  - E. Anti-Inflation Efforts; Early 1969
  - F. The Failure to Devalue
  - G. Austerity Tax Measure of October 1969
  - H. Reaction To The Measure

TABLE OF CONTENTS - continued

- I. Inflation and Speculation in 1970
  - 1. The Rice Market
  - 2. Import Activity
- J. Verdict on The Austerity Tax; Skulduggery at The Customs
- K. Gap Results, 1969-70
- X Economic Reform and Progress, September 1970 - March 1972
  - A. A Change in Economic Leadership
  - B. Interest Rate Reform of September 1970
    - 1. Background
    - 2. Measure of September, 1970
    - 3. Aftermath of The Measure
  - C. Measures of October 3, 1970
  - D. Effect of the October Measures
    - 1. Degree of Devaluation
    - 2. Accommodation Rate
  - E. Reform Measures of 1971
  - F. Exchange Rate Considerations
    - 1. Devaluation and tariff simplification.
    - 2. GVN - CIP rate differential
    - 3. Dual licensing
    - 4. Open General Licensing
    - 5. Subsidies and protection
  - G. Economic Activity, 1971
    - 1. Agriculture
    - 2. Industry
      - a. Industrial Development Bank
      - b. Divestiture
    - 3. GNP and goods availability
    - 4. Manpower and employment
    - 5. Money supply and inflation, 1971
      - a. Monetary Gap
      - b. Prices
    - 6. Banking and credit
      - a. Saigon banks; role in deficit financing
      - b. ADB and rural banks
    - 7. Balance of Payments
    - 8. Exports

TABLE OF CONTENTS - continued

- H. U.S. Aid
  - I. January - March, 1972
- XI Misfortune Befalls, 1972
  - A. NVA Offensive
  - B. U.S. Force Withdrawal
  - C. Decline in U.S. Aid
  - D. Import Prices
  - E. Rice
  - F. Economic Activity
  - G. National Income
  - H. Self-help Measures
    - 1. Exports
    - 2. Tax Reform
    - 3. Other Self-help Measures
  - I. Balance of Payments
  - J. Monetary Gap and Inflation
    - 1. Monetary Gap
    - 2. Prices
- XII Recession, Aid Decline, and The Struggle For Self-Sufficiency, 1973-74
  - A. U.S. Withdrawal Completed
  - B. Increase in World Prices
  - C. U.S. Aid
  - D. Other Donor Aid
  - E. Balance of Payments
    - 1. 1973
    - 2. 1974
  - F. Imports, Nominal and Real

TABLE OF CONTENTS - continued

- G. Efforts To Conserve Foreign Exchange
  - 1. Non-essential Imports
  - 2. Other Import Reductions; Sugar and POL
- H. Resource Transfers
- I. Manufacturing Activity
- J. Agriculture, Forestry and Fishing
  - 1. Rice
    - a. The Rice-Fertilizer Price Issue
  - 2. Other crops
  - 3. Forestry
  - 4. Fishing
- K. Land Reform
- L. Exports
- M. Foreign Investment
  - 1. 1973
  - 2. 1974
- N. Income and Employment
- O. Money Supply and Inflation
  - 1. 1973
  - 2. 1974
- P. Banking and Credit
  - 1. Credit
  - 2. Savings
  - 3. Interest Rate Policy
    - a. Overall rate level
    - b. Treasury Bill rates
    - c. Development lending
- Q. GVN Expenditures
  - 1. 1973
  - 2. 1974
- R. GVN Revenues
  - 1. 1973-74 Results
  - 2. Value Added Tax
- S. Deficit Financing

TABLE OF CONTENTS - continued

- T. Economic Development
  - U. Exchange Rate Policy
    - 1. Official Rate
    - 2. GVN - CIP Differential
    - 3. Export Rate
  - V. The Great Debate; Monetary vs. Cost Inflation
  - W. GVN Economic Organization
- XIII The End; 1975
- A. Economic Events, January - March
  - B. The Fiscal Outlook
  - C. The Tax Dilemma
  - D. The Monetary Trap Complete
  - E. April
- XIV. A Footnote on Corruption
- XV Conclusion

TABLES

- 1. U.S. Aid & Import Support, 1954-75
- 2. U.S. Import Support, Nominal and Real, 1964-74
- 3. Consumer Prices, 1954-74
- 4. Money Supply and Prices, 1957-74
- 5. Money Supply and Savings, 1957-74
- 6. Credit, 1955-75
- 7. GVN Budget, 1964-75
- 8. GVN Official Exchange Reserves, 1955-74
- 9. Simplified Balance of Payments, 1964-74

TABLE OF CONTENTS - continued

10. Commercial Import Payments, Nominal and Real, 1964-74
11. Paddy Available For All Uses, 1964-74
12. Official Exchange Rates, 1954-75
13. Black Market and Legal Exchange Rates, 1965-74
14. Black Market Premium/Discount for \$10, 1964-74

## FORWARD

This report represents an attempt to summarize economic activity, and A.I.D.'s influence on policy-making and economic developments, during the period of U.S. involvement in Viet Nam, 1954-75. In its consideration of the U.S. Aid program, the report confines itself almost exclusively to economic aid, as distinguished from the Military Assistance Support Funding Program (MASF) which of course was a great deal more important in terms of dollars expended. MASF-funded activities are considered in areas where a direct economic impact could be observed, including especially the piaster purchases of the Military Assistance Command Viet Nam (MACV) and its successor agency, the Defense Attache Office (DAO), to finance their in-country activities, and it is recognized that MASF had an important indirect economic effect in the provision of infrastructure - roads, harbors, airports, etc. However, in the interests of keeping the scope of this paper within bounds, these indirect effects of MASF-funded activities, as well as the direct support of the war effort, are not dealt with.

The report was of course undertaken after the fall of Viet Nam, which has meant the unavailability of the economic files of USAID/Saigon, all of which were lost. Fortunately, a good deal of material was available in A.I.D./Washington, enough to make this effort possible. However, it has not been possible to obtain complete data series on all topics, nor in many cases to be very precise on dates of key events. Apart from the 1954-64 period on which the available material was very skimpy, the principal data problem has concerned 1974.

92

Still on the subject of data, the usual caveat of writers on Viet Nam applies here. That is, whatever the area of activity, one seldom encounters two data series that agree with one another. The writer has included the series that he considers most reliable, has reconciled conflicting series to the best of his ability, and has tried to maintain consistency within the confines of this report. No other claims are offered.

## I. Introduction: Background to U.S. Involvement

American influence on the Vietnamese economy can be dated from the late 1940s with the channeling of large scale military and economic aid through France. A portion of Marshall Plan aid was earmarked by the French for their dependent overseas territories. Though indirect in nature, U.S. assistance was critical to the ability of the French to sustain their effort during those years.

Direct U.S. involvement began with the establishment of the Special Technical and Economic Mission (STEM) in 1950. STEM operated in cooperation with the French, providing assistance to the Associated States of Indochina, including North Viet Nam. The early program involved technical assistance and advice in such projects as development of marine fisheries, improvement of the Port of Saigon, civil aviation, health services, adult literacy training, and development of government information services. It was limited in budget as well as in scope.

Direct U.S. involvement on a large scale began with the establishment of the U.S. Operations Missions (USOM) following the signing of the Geneva Accords in July 1954. At its inception, USOM's function was to plug the financial gap left by the departing French and to assist in the transition from dependent territory status to an independent state. To these tasks was added that of coping with the flood of refugees from the North.

## II. The Vietnamese Economy in 1954

South Viet Nam in 1954 was a predominantly agricultural country with a largely rural population of about 11 million. Its per capita GNP of

about \$160 placed it solidly in the ranks of the less developed, but well above the poorest in terms of living standards. Rice and rubber, though having suffered severe production declines due to the war, still provided the backbone of the economy and accounted for about 85 percent of the country's exports. Although below its export totals of pre-World War II years, Viet Nam along with its Southeast Asian neighbors of Cambodia and Thailand was one of the world's leading rice suppliers.

The country produced a wide range of secondary crops, such as peanuts, corn, tea and coffee, sugar and fruits in great abundance. There was a fairly plentiful fish supply. There were virtually no known mineral resources, save for the coal deposits at Nong Son in the northern part of the country. Industry had been very little developed, consisting of small-scale light manufacturing, mainly in the Saigon-Cholon area, employing about 40,000 workers. The country's transportation network had been fairly well developed but had suffered severe war damage, with some 60 percent of the road and one-third of the rail network having been destroyed.

For all its natural wealth in agricultural resources and its rice exports South Viet Nam was not self-sufficient in food, importing substantial amounts of wheat, sugar, and dairy products. Its potential in agriculture was at least partly offset by the rapid population growth and more than matched in the near term by the heavy influx of refugees from the North.

The foreign trade account was heavily in deficit, with exports covering 20 to 30 percent of imports. The gap had been covered during 1950-54 by French--ultimately American--aid.

95

### III. Early Difficulties

The new state of South Viet Nam faced a staggering array of difficulties at the outset. The refugee migration from the North variously estimated at 800-900,000 persons, was to add some eight percent to the country's population in a ten-month period of 1954-55. At the same time, the withdrawal of the French meant the loss overnight of a major economic prop. The French had employed some 40,000 people in arsenals and workshops around the country and 120,000 Vietnamese had served in the French army, few of whom were to remain in the reconstituted national army. French civil servants and technicians were leaving the country in large numbers and the government meanwhile had to cope with severe technical problems involved in the shift to independent country status. The government itself faced intense internal opposition from three dissident sects; indeed, the survivability of the untried Diem government was very much an open question.

To meet the immediate problems of the new state, the U.S. Congress appropriated in fiscal 1955 \$322.4 million in economic aid. Of the total, \$253.7 million was allocated to the Commercial Import Program (CIP) to cover Viet Nam's budget and balance of payments deficits. Not only was this to be the largest one year A.I.D. authorization until 1966, but viewed in real terms (after allowance for increases in world prices over the years), the CIP portion of the program would be the largest ever except for one year, 1966.

Project and other aid in FY 1955 amounted to \$66.5 million of which \$57 million was applied to refugee assistance. The refugee program

received another \$37 million in FY 1956 after which time this form of assistance was terminated, at least for the time being.

A major portion of USOM's effort in 1954-55 involved assisting the Vietnamese in the transitional problems brought on by the departure of the French and the need to develop a new administrative structure overnight. Not the least of these problems was the closing of the Tripartite Institute d'Emission, which left the country temporarily without a bank of issue. With USOM assistance the National Bank of Viet Nam opened as a Bank of Note Issue on January 1, 1955.

#### IV. 1954-64

If the overall period of U.S. direct involvement from 1954-75 divides naturally at the year 1964--the last year before the U.S. presence was to take a quantum leap forward--the 1954-64 period itself could be divided almost as neatly into two periods, before and after 1960. The years 1955-60 were marked by relative security, financial stability, and a fairly impressive measure of economic development. The period 1961-64 on the other hand was marked by rising Viet Cong insurgent activity, increasing budget deficits, mounting inflationary pressures, and for the most part, economic stagnation.

#### A. Economic activity

For the reasons stated above, the available indicators of economic activity can be reviewed most conveniently by considering separately the periods 1955-60 (from here on we will speak of 1955 as the starting point since this was the first full year of relative peace) and 1961-64.

1. 1955-60

Production data from Viet Nam have always been of questionable reliability, and they seem to have been especially so for the 1955-64 period. Partly for that reason observers have differed in their assessments of economic progress, or lack of it. It seems to be beyond doubt, however, that the 1955-60 period was one of more rapid growth than any period that was to follow. In part this was a catch-up process, a making up for losses suffered during the prolonged period of warfare, but the record seems to have been impressive; an indication, perhaps, of what could be achieved given relatively peaceful conditions.

Rice production rose rapidly as the cessation of fighting enabled abandoned lands to be put back into production. By 1960, the area under cultivation had reached 2,400,000 hectares, up from 1,660,000 in 1954. Rice production was reported as 5,092,000 MT of paddy, which compares with 2,080,000 MT in 1954 and 2,767,000 MT in 1955. The 1959 and 1960 production figures are questionable since they imply huge increases in yield (from 1.2 MT per hectare in 1958 to 1.9 in 1959 and 2.1 in 1960), but undoubtedly Viet Nam's rice output had surpassed pre-Indochina War, if not pre-World War II, levels. Rice exports in 1960 were 340,000 MT, below pre-World War II levels, but still high enough to set a post-Indochina War record and a figure not to be reached again. Rubber production, benefiting from the cessation of major hostilities rose steadily throughout the period. At 68,000 MT for the major plantations (which accounted for roughly 85 percent of total output), rubber output in 1960 was 33 percent above the 1954 level.

98

Manufacturing activity gained little ground during 1955-60 in terms of final output; the index of manufacturing production in 1960 had risen a modest 16 percent from its very narrow 1955 base. However, this period did see the implementation of a 1957-62 Development Plan which, while favoring agriculture ahead of industry, nevertheless accorded more attention to industry than theretofore. The emphasis was on import-substitute industries and good progress was made in the areas of textiles, paper, and cement. Other industries started (though whether before or after 1960 is not clear from available records) were pharmaceuticals, chemicals, plastics, and metal working. The government's proclaimed intention was to base new industries on the country's natural resources, but in practice they tended to become heavily import dependent. Export development was not a factor. Other developments of note during this period, both in 1957, were the promulgation of a new Foreign Investment Law that, on paper at least, appeared to improve the climate for foreign investors, and the establishment of an Industrial Development Corporation financed largely by a \$10 million contribution from USOM.

2. 1961-64

Terrorism had begun to recur on a rising scale by late 1959 and was a growing if not yet disruptive problem in 1960. The real shift to large scale terrorism with decisive economic implications came with the formation of the National Liberation Front in December 1960. The rise in insurgent activity was to impact far more heavily on the countryside, and agricultural activity, than on the cities where, in fact, the manufacturing sector made significant progress.

Rice output continued to expand during this period, but less rapidly than in the previous six years. By 1964 both the area planted and rice output were about ten percent above their 1960 levels. Rice exports were 323,000 MT in 1963 (\$36 million) and 49,000 MT (\$5.3 million) in 1964. The area under cultivation in the 1964-65 crop year was at a level not to be seen again until 1971.

Agricultural output as a whole leveled off during 1961-64. Rubber production held within a range of 68-79,000 MT.

Contrary to the relative stagnation in agriculture, manufacturing production enjoyed relatively rapid growth during this period. The largest single accomplishment was completion of the Ha Tien cement plant with an annual capacity of 250,000 MT. Other industries started during 1955-60 came on line during 1961-64, including, in the Saigon-Cholon area, a Michelin tire plant, a glass plant, and a paper plant. Development of the textile industry was significant with major foreign exchange savings effected. Overall, and again, the data are suspect both in themselves and also by virtue of the narrow base from which the index was constructed, the index of manufacturing production which stood at 100 in 1956 and 116 in 1960, was at 179 in 1964. The 1960-64 gain was one of 54 percent. Employment in manufacturing had reached approximately 100,000 in 1964, more than twice the 1954 level.

#### B. Fiscal and Monetary Developments

Data on actual government expenditures (as opposed to budget data) are not available for the years prior to 1961. However, it is known that budget deficits were largely covered by foreign aid and National Bank

borrowing was either nil or at a very low level. The principal element of stability was the relatively constant size of the armed forces, which held within a range of 242-248,000 throughout the 1955-60 period. With the formation of the National Liberation Front in December 1960 and the concomitant rise in insurgency, the armed forces began a rapid build-up. The force level rose to 305,000 in 1961 and from there steadily to 514,000 in 1964. Civil service employment also rose rapidly, from 110,000 in 1961 (first year for which data are available) to 143,000 in 1964. Overall, government employment reached 657,000 in 1964 having increased 58 percent in three years.

The burgeoning payroll was naturally reflected in overall government expenditures, which rose by 77 percent in the two years 1961-63. Revenue collections, meanwhile, lagged far behind, as did the contribution from foreign aid. The result was an increasing deficit to be financed by monetary means as follows:

GVN BUDGET 1961-64

(\$VN billions)

	<u>1961</u>	<u>1962</u>	<u>1963</u>	<u>1964</u>
Expenditures	16.3	22.0	28.9	28.9
Revenues	<u>-11.6</u>	<u>-11.3</u>	<u>-11.9</u>	<u>-13.0</u>
Deficit before foreign aid	4.7	10.7	17.0	15.9
Foreign aid	<u>- 4.7</u>	<u>- 7.7</u>	<u>- 7.4</u>	<u>- 6.4</u>
Deficit	- 0	3.0	9.6	9.5

Money supply, which had been relatively stable until 1958, rose 134 percent during 1959-64. Consumer prices moved much more slowly, rising only 24 percent in the same period. The disparity between the growth of money supply and the rise in prices for the entire period 1955-64 was

remarkable. It reflected idle capacity with substantial unemployment in the economy, including the large numbers discharged from French employ and the refugees moving South. Also a factor in the dampening of inflationary forces was an increasing monetization of the country's trade and, especially during 1955-60, a fair measure of economic growth. By 1964 the slack in the economy was increasingly being taken up, helped along by the rapid growth of the armed forces. The country was to have only another year or two of breathing space before inflation would become the dominant fact of economic life.

C. Balance of payments

The available foreign trade data are so contradictory that it seems best to summarize the balance of payments in terms of annual averages, taking several years at a time. A presentation of this nature will also enable the reader to see rather easily the change in trade and aid magnitudes as between the 1956-60 and 1961-64 periods:

Simplified Balance of Payments (Annual Averages) 1955-64  
(\$ U.S. millions)

	<u>1956-60</u>	<u>1961-64</u>
A. Exports	70	63
B. Imports, c.i.f.	<u>-245</u>	<u>-292</u>
C. Trade deficit	-175	-229
D. Services	- 21	4
E. Misc. transfer payments and capital	13	24
F. Errors and omissions	<u>1</u>	<u>1</u>
G. Balance before foreign aid (C+D+E+F)	-182	-200
H. U.S. aid	208	182
I. Change in foreign assets (inc.-) (of which gold and foreign exchange)	- 26 (- 23)	20 ( 18)

Comparing 1961-64 with 1956-60, we can observe the following: a substantial rise in the trade deficit, brought on mainly by higher imports; a partially offsetting improvement in the services account (owing partly to rising piaster purchases by the American sector), but a higher deficit before foreign aid nonetheless; a decline in the level of American aid; and a change from a rise to a decline in the level of National Bank reserves. NBVN holdings of gold and foreign exchange rose from \$125 million at the end of 1955 to \$216 million at the end of 1960, and were then drawn back down to \$136 million by the end of 1964.

D. U.S. Aid directions

The composition, as well as the magnitude, of the U.S. aid program changed significantly after 1960 as can be seen in the following summary for the 1955-64 period:

Composition of U.S. aid  
( \$ U.S. millions )

<u>Annual Averages</u>	<u>1955-60</u>	<u>1961-64</u>
CIP	179	103
PL 480 Title I (Food for Peace)	11	39
Project and Other	42	40
Total	<u>232</u>	<u>182</u>

As can be seen, the principal shifts were a sharp drop in the level of the CIP, only partially offset by a rise in Food for Peace, the sale of surplus U.S. agricultural commodities. The Project program held its own during the ten year period.

The major development in the administration of the USOM program was a shift in emphasis from concentration on economic assistance and development

to a focus on counterinsurgency. While the shift in emphasis can be dated as of 1961, it became more or less official with the formation of the Office of Rural Affairs--the forerunner of CORDS--in June 1962. With the establishment of the ORA, USOM for the first time located a large element of A.I.D. officers in the area of field operations with sub-offices in the four military regions and on down to the province level. Concomitant with the establishment of ORA was an increasing emphasis on the Public Safety program, another major element of the counterinsurgency effort. Economic and other technical assistance projects were not discontinued, merely overshadowed in the new emphasis on counterinsurgency.

E. Exchange Rate Developments

There was one formal devaluation during the 1955-64 period, in January 1962. Lesser changes, short of a full-fledged devaluation, occurred in 1957.

1. 1955-61

The official rate of exchange, established in May 1953, was 35 piasters to the dollar. A "free" rate applicable to financial transactions, existed at VN \$73.5:1. The official rate applied to A.I.D.-financed imports until 1957 when a production tax of five or seven piasters, depending on the commodity, was added to bring the effective A.I.D. rate to 40 or 42:1. A very few GVN imports moved at the official rate; most were subject to a stabilization surtax that brought their effective rate to from 74 to 110 to 1, depending on the year and the commodity. Exports of rice were subject to the official rate until 1957. Exporters of other commodities were

allowed to retain abroad a certain percentage--varying by commodity--of their foreign exchange proceeds. From 1957 on, all export proceeds were repatriated, 65 percent at the official rate and 35 percent at the "free" rate, for an effective rate of 48.48:1.

2. After January 1, 1962

As of January 1, 1962 all exports and imports became subject to a Consolidated Surplus tax of 25 piasters to the dollar, which replaced pre-existing special taxes. This tax, commonly known as the "five sevenths tax", brought the basic trade rate to 60:1. In fact, rice was the only export product to move at 60:1. Rubber exports were subject to a tax which lowered the piaster yield to 48.65:1. Other exports received premiums ranging from five to 15 piasters per dollar. On the import side, less essential imports became subject to greatly increased customs and austerity duties. Finally, there was no change either in the official rate or the financial rate of 73.5:1. By 1962, however, the official rate applied only to U.S. purchases of piasters for official use.

3. Summary; appropriateness of the rate level

Owing to the complexity of the rate schedule, it is impossible to measure precisely the extent of the 1957 and 1962 devaluations. At one extreme, the A.I.D. import rate, the devaluation amounted overall to 71 percent. At the other, the official and financial rates, it was a devaluation of zero. Exports were somewhere in between, depending again on the commodity. The following is a summary of these changes. It assumes that the privilege granted to some exporters of retaining a percentage of their earnings abroad during 1954-57 was worth 73.5 piasters to the dollar,

i.e., equal to the financial rate. Given the array of customs and austerity taxes applicable to GVN financed imports, no attempt was made to measure an effective GVN import rate.

Effective Exchange Rates 1954-66  
(piasters per dollar)

	<u>1954-57</u>	<u>1957-62</u>	<u>1962-66</u>
Official	35	35	35
A.I.D. import	35	40-42	60
Financial	73.5	73.5	73.5
Exports:			
Rice	35		60
Rubber	40-42	48.48	45.65
Other	45.8-73.5		65-75

It seems certain that the piaster was overvalued--perhaps heavily so--at least until 1962. The devaluation of that year may have caught the piaster up on an international parity basis, but even this is doubtful. Overvaluation was at least partly reflected in the piaster cross-rate in Hong Kong which during 1955-62 fluctuated in the range of 82:1 to 92:1. After January 1, 1962, the Hong Kong rate moved up moderately holding in a range of 90 to 100 to the dollar until 1964 when it ended the year at 121:1. Overvaluation seems to have been reflected in the performance of exports which in fact were not an area of priority importance to the GVN during these years. Exports of products other than rubber and rice--which admittedly were not very responsive to exchange rate movements, at least in the short run--were \$11.7 million in 1957 (first year for which such data are available) and did not get back to that level until 1972.

F. GVN economic policies

There is unfortunately nothing in the A.I.D. records of major economic policy issues and their disposition during the 1954-64 period. Apart from being further removed in time, which has meant considerable loss of records, this again was a period that relative to 1965-75, has been slighted by the analysts. A certain amount is known, however, of the policies and attitudes of Vietnamese economic officialdom, and more can be inferred from the record.

The Vietnamese were then, and were to remain, essentially conservative in their economic thinking. This was especially notable in the fiscal area, an inheritance from the French who inculcated a balanced-budget, project approach. Only the exigencies of the increasing warfare were to impel them to deficit financing, but even then the GVN would never become profligate in their approach to spending.

Conservatism was reflected also in their approach to planning. The \$500 million allotted to the 1957-62 Plan could be contrasted with Nguyen Hanh's estimate of \$160 million as the amount needed annually to relieve unemployment in the Saigon-Cholon area alone. It was reflected also in the GVN's demonstrable predilection for accumulating currency reserves. The decline in reserves during 1961-64 could be ascribed to a temporary reduction in U.S. aid, but when the aid level was steady, as it was during 1955-60, reserves rose strongly. (The rise in reserves, from \$125 million at the end of 1955 to \$216 million at the end of 1960 may well have been a factor in the subsequent reduction of U.S. aid during 1961-64).

Economic policy, especially in the approach to foreign investment, reflected a strong element of nationalism, not surprising considering the long period of Chinese and French domination. While the Foreign Investment Law of 1957 contained all the right investment incentives, and President Diem professed to welcome foreign investors, the government frustrated its proclaimed intentions by taking majority ownership in all of the larger new business enterprises. Moreover, investment procedures continued to be strangled in a bewildering array of red tape. The security situation was also a factor, but the fact remains that foreign investment was insignificant throughout this period.

The Vietnamese were extremely laggard in export development. This was evident in the absence of any attention to exports in the 1957-62 Plan. Exchange rate policy appeared to favor certain exports, in that they were accorded rates that were favorable relative to the other exchange rates in effect, but as discussed above, even at the preferred export rates, the piaster appears to have been overvalued throughout this period.

The Vietnamese may have felt that they could not do very much about their exports given the supply inelasticity of their major export commodities, rice and rubber (if so, the events of 1971-74 were to prove them wrong), but it is likely that another factor accounted for both their export and exchange rate policies; namely, the easy availability of American aid. Given U.S. aid, development of exports may not have seemed very necessary. At the same time, maintenance of a low (overvalued) exchange rate was preferable in that it minimized the piaster cost of imports, thereby contributing to price stability, and maximized the dollar earnings

from U.S. purchases of piasters.

As stated earlier, the policies and attitudes suggested here are to a large extent inferred from the record, rather than documented as such. What is interesting is that most of the elements of the situation were to persist throughout the period of U.S. involvement. So too would the attitudes until the U.S. force withdrawal and the threat of a U.S. aid reduction would compel a rethinking.

V. The Vietnamese Economy in 1964

Although considerable change took place in the first decade following the signing of the Geneva accords in 1954, the impact of the war and of the American presence on the country's economic life had barely been felt in comparison with what was to follow.

In 1964 Viet Nam's population of 15 million was still about 80 percent rural. Saigon, the major city by far, had a population of less than a million. Rice production was at the highest level since pre-World War II years and rice was still being exported. The only industries of significance were textiles, paper, and cement, all government owned, and little investment was taking place, either foreign or domestic. There was widespread unemployment - more especially, underemployment--and the economy was largely stagnant.

On the political front, the assassination of Ngo Diem Diem in November 1963 had been followed by a period of uncertainty as rival politicians jockeyed for power. In response to the growing insurgency, the armed forces had increased to half a million men. U.S. military personnel in-country numbered only 23,000 at year end. Deficit spending had become an increasing problem, but had not yet led to significant price inflation.

109

Externally, the country had long since become dependent on U.S. aid to finance needed raw material and capital goods imports.

As an indicator of the changes taking place, the share of the government sector in the total Net Domestic Product of Viet Nam rose from 15 percent in 1960 (first year for which such data are available) to 21.3 percent in 1964. The share of the government and services sectors together had risen from 56.3 percent to 70.7 percent. By 1972 these shares would be 34.1 percent and 78.1 percent, respectively.

#### VI. The Import Economy, 1965-67.

The period 1965-67 in Viet Nam was unlike anything ever experienced by an underdeveloped country. An enormous foreign presence was superimposed on a small, basically rural economy in a short span of time. To combat the resulting inflationary pressures, the U.S. fostered a deliberate policy of maximizing imports. As a result, along with the inevitable, far-reaching economic distortions, the country enjoyed, for a time, a substantial degree of prosperity.

#### A. Inflationary Pressures, 1965-66

Prior to 1965 inflation had been a matter of little concern. As noted earlier, deficit spending had been on the rise since the beginning of the GVN force buildup in 1961 but the slack in the economy was sufficient to absorb the increasing demands on it with little repercussion in terms of prices. Consumer prices, as measured by the National Institute of Statistics (NIS), averaged only 3.2 percent higher in 1964 than in 1963. But the slack, in terms of underemployed manpower and resources, was being used up. The combined effects of U.S. and GVN force buildups and declining

domestic production were drastically to alter the situation during the next few years.

1. U.S. Force Buildup

With the decision to commit U.S. ground forces on a large scale, the American buildup proceeded at a rapid pace. U.S. military forces in-country rose from 23,000 at the end of 1964 to 184,000 in 1965 and 485,000 at the end of 1966. The force level was to rise by only another 57,000 in the two following years leading to the peak level of 542,000 reached in January 1969.

Concurrent with the buildup in the U.S. military was the growing demand by the Department of Defense (DOD) and its contractors for Vietnamese citizens to work on construction projects, drive trucks, unload ships, etc. By the end of 1966 the U.S. sector employed 142,000 persons, whereas it had employed only a handful two years earlier. Nor did this count the indirect employment of countless others--probably equal in number to those directly employed--engaged in supplying and catering to the U.S. forces, from the employees of the oil companies to laundry workers, car washers, and bar girls.

The impact of the U.S. forces and of the Vietnamese employed in the U.S. sector was not to be inflationary in the long run. This is because, eventually, the dollars spent by the Department of Defense (DOD) to obtain their piaster requirements would be rechanneled into imports which, because they were taxed, had a deflationary effect that more than offset the original inflationary impact. However, the spending to import absorption process worked with a time lag which amounted to six months under the best of circumstances, but which might as well have been infinite in the special conditions of 1965-66. As will be seen in the discussion of the port congestion

problem of those years, the time lag in question was greatly lengthened by the fact that the Port of Saigon could not accommodate the available A.I.D. goods, let alone all of the additional goods that might have been financed by the available GVN-owned foreign exchange.

The rise in the U.S. force level was, then, almost wholly inflationary during this period. The increasing U.S. sector employment--both direct and indirect--was less so, or less obviously so, since those employed were producers. Since, however, their production consisted almost entirely of services consumed by the U.S. forces themselves, their principal economic effect was as a partial offset to the spending of the American troops. Meanwhile, their employment at bases, camps, and in the multitude of U.S. service industries meant a real diversion from previous production of goods and services for the economy proper.

## 2. GVN Employment

The GVN armed forces continued to expand, though somewhat less rapidly than before, rising from 514,000 at the end of 1964 to 562,000 at the end of 1966. More significant was the rise in civil service employment, which rose by 76,000 to 219,000, including police, in 1966. Altogether, public sector employment, military and civil, rose by some 124,000 during this period.

## 3. Diversion of Resources From Production

The shift of manpower resources to GVN and U.S. sector employment was accompanied--and aided--by a movement of the population as a whole away from increasingly insecure areas of the countryside into the cities. Viet Nam's population was to go from a ratio of about 80 percent rural,

20 percent urban in 1964 to one of about 60-40 by the end of U.S. involvement. The process can be seen as inevitable, and even desirable, in the sense that it was necessary to provide the manpower needed by the war related industries, such as construction and stevedoring, but it had a severe impact on agricultural output. Between 1964 and 1966, some 200,000 hectares of rice land were to go out of production; output would decline by 800,000 MT of paddy, or 16 percent. Agricultural output as a whole would decline by a like percentage.

#### 4. The A.I.D. Response

A.I.D. Administrator David Bell visited Viet Nam together with Secretary McNamara and the State Department's Chairman of the Inter-Agency Viet Nam Coordinating Committee, Michael Forrestal, early in 1964. The principal result of the mission was to persuade the GVN to adopt a "resources" or "foreign exchange gap" basis for estimating U.S. aid requirements. Previously, both levels and composition of import requirements were calculated insofar as possible, on the basis of the projected budget deficit. Given the orthodox attitudes of the old line, colonially-trained GVN officials toward deficit spending, it was felt that this approach was allowing defense requirements to go unfunded, thereby inhibiting the war effort. Under the new approach, the GVN was urged to increase its defense budget as required to support the war effort, permit deficit financing to the extent tax revenues and previous CIP counterpart generations<sup>a/</sup> did not

- a) Under Commercial Import Program (CIP) procedures an importer paid for an imported item in piasters at the prevailing rate of exchange. Payment was made to a counterpart fund at the National Bank through an intermediary bank. Most of the counterpart, excepting a portion retained for U.S. uses in-country, was in turn transferred to the GVN which applied it to the budget as foreign aid revenues.

suffice, and leave the level and composition of imports to market forces. U.S. aid would supply the financing to the extent GVN-owned foreign exchange reserves were insufficient.

The changeover in approach and attitude was not accomplished overnight, but at least the stage had been set for the increase in the level of U.S. aid that was to follow. Faced with the prospect of runaway inflation in 1965 U.S. economic policy makers opted for a rise in imports sufficient to hold the inflation at least reasonably well within bounds. To accommodate the increase, as well as the other demands being created by the counterinsurgency effort, both the overall A.I.D. authorization and the portion of the authorization allocated to the CIP program, more than tripled in size between 1964 and 1966.

U.S. A.I.D. Authorizations, 1964-66  
(U.S. \$ millions)

	<u>1964</u>	<u>1965</u>	<u>1966</u>
CIP	113.0	150.0	399.3
Food for Peace	59.1	49.9	143.0
Project and Other	<u>52.7</u>	<u>75.0</u>	<u>194.2</u>
Total	224.8	274.9	736.5

5. Progress of Inflation

Before assessing the progress of inflation it will be useful here briefly to review the technique by which inflation was commonly measured in Viet Nam.

a. Method of analyzing inflation; the monetary gap. The causes of the inflation that developed during 1965-66 are easy enough to identify; very briefly a huge increase in public expenditures accompanied by a diversion of resources from production. But precise measurement of the process

proved difficult for analysts given the unusual processes at work and the inadequacy of the available national accounts data. To resolve their difficulties, economists developed a technique of monetary analysis known as measuring the "gap". The gap, as understood in this context is the increase in money supply predicted to take place in a given time period in the future, or which actually took place in the past. Gap analysis did not provide a direct measure of price inflation since price increases seldom corresponded to increases in the money supply, especially in the short run. However, it did provide an estimate--or an ex-post view--of the inflationary forces at work.

The basic elements of the gap equation are simple, if often difficult to measure. They are the forces operating to expand or contract the money supply, defined as demand deposits and currency in circulation. In the Vietnamese context, these could be identified--in a simplified way-- as follows:

Expansionary factors:

- GVN expenditures
- exports
- invisible expenditures, including the piaster expenditures of foreign governments and their troops
- private credit expansion

Contractionary factors:

- GVN tax collections, including customs
- imports
- invisible imports
- private savings

b. Inflation, 1964-66. With this as background and keeping in mind that declining real output during this period was also a factor, the

115

monetary factors in the inflation of 1965-66 can now be assessed:

<u>Billions of Piasters</u>			
	<u>1964</u>	<u>1965</u>	<u>1966</u>
<u>Expansion</u>			
GVN budget	28.6	44.1	59.0
U.S. sector expend	1.9	12.6	37.5
Credit and Other	<u>7.2</u>	<u>8.6</u>	<u>33.1</u>
Total	37.7	65.3	129.6
<u>Contraction</u>			
GVN revenues:	13.2	15.5	38.6
(Domestic taxes)	(8.1)	(9.7)	(17.3)
(Import taxes)	(5.1)	(5.8)	(21.3)
Imports	13.8	17.1	47.3
Other	<u>3.0</u>	<u>5.1</u>	<u>9.4</u>
Total	30.0	37.7	95.3
<u>Errors and omissions</u>	-2.6	-7.4 <sup>b/</sup>	-16.4 <sup>b/</sup>
Money supply increase (Gap)	5.1	20.2	17.8
Money Supply Inc. (%) <sup>a/</sup>	23%	74%	37%
Cost of Living Inc.	6%	36%	61%

a) National Institute of Statistics (NIS) for working class families.

b) Owing to the imprecision of the data and the varying lead and lag times involved, it was seldom possible to arrive at a precise reconciliation of all of the factors involved in the money supply increase. The "errors and omissions" category was especially large in these two years: in 1965, because the gap technique had as yet been little refined; in 1966 because of especially difficult data problems relating to the devaluation of that year.

Looking first at the bottom lines, we see that money supply rose by 74 percent in 1965. Price inflation was a far more moderate 35 percent largely because, for part of the year at least, there still existed some slack in the economy as it moved toward full employment. By 1966 resources were fully employed in all but the frictional sense, and the inflationary overhang had its effect. Money supply, restrained by the import surge combined with the devaluation in June of that year, was held to an increase

of 37 percent but prices shot up by 61 percent. It was to be the worst inflation year of the U.S. involvement until 1973.

The principal factors in the early inflation can be seen from the above data. On the expenditure side, GVN spending was initially more important than U.S. expenditures. In 1965 the massive effort to construct bases for the troops was still in the organizing stage; actual U.S. expenditures were small until 1966. Revenue collections lagged far behind combined GVN and U.S. spending, and the percentage increase in revenues lagged behind the rate of inflation itself. The inelasticity of domestic tax revenues with respect to price inflation was caused at least in part by the fact that most Vietnamese indirect taxes were levied on a specific as opposed to an ad valorem basis. It became evident early on that if tax revenues were to keep pace with inflation, tax rates would have to be frequently adjusted.

Perhaps the most interesting development was the early lag in imports notwithstanding the demand inflation that was taking place, the ready availability of import financing and the conscious effort of policy makers to maximize imports. The explanation lay first in the mechanics of the CIP itself, and later, in the port congestion of 1965-66.

#### 6. Imports, 1965-66; Port Congestion

In U.S. dollar terms, payments for imports (which corresponded closely to actual arrivals) rose from 233 million in 1964 to 572 million in 1966. These figures lagged far behind the combined A.I.D. and foreign exchange availabilities for the period. As partial witness to this point, GVN holdings of gold and foreign exchange rose from \$135.7 million at the end

of 1964 to \$300,7 million at the end of 1966.

Initially the import lag was a matter of the normal lead time between ordering and arrival of goods under the CIP. Even under normal circumstances it took seven to nine months from the time an importer placed his order in Saigon through the paperwork procedures and shipping time, to arrival in Saigon. By the end of 1965, and all through 1966, a jam-up of facilities in the port of Saigon was adding to the problem so that goods were delayed in reaching the market place for months after the ships carrying them arrived in Saigon.

The results are evident in a comparison of authorization and import payments data for 1966. The combined funds available under the CIP and PL 480 Title I (Food for Peace) programs for the 1966 fiscal year was \$542 million. Import payments for calendar year 1966 (six months later) were \$335 million, thus, a buildup in the aid pipeline of some \$200 million was added to the GVN exchange reserve buildup of \$128 million in the same year. As 1966 began, it was evident that import financing alone could not stem the inflation given the other forces at work.

7. Honolulu Conference, February 1966; Tax Increases

Top U.S. and GVN economists met in Honolulu in February 1966 to map strategy for countering the inflation. The decision was taken to make an effort to raise taxes. Several new taxes were accordingly introduced in March which together were designed to raise an additional VN\$ 5 billion in annual revenues. Further increases were planned but had to be put off for political reasons by April. The Buddhist "struggle" movement was under way.

8. The Devaluation of June 1966

The devaluation of June 1966 was undertaken primarily as an anti-inflation measure, but the need to counter inflation was not the sole motivation. The effective rate for imports had been set at 60:1 since January 1, 1962 and inflation since that time had made imports increasingly cheap relative to domestically produced goods and services. Together with the port tie-up, which was contributing to a scarcity of goods in the market, those importers able to obtain licenses and get delivery on goods were making large profits. Indeed, the "windfall" profits of importers was one of the leading topics of the day in economic circles. From the standpoint of equity as well as finance it made sense to bring those profits into the Treasury.

From the economic standpoint there appeared by now to be no other way to effectively attack the inflation problem. Public sector expenditures were rising strongly, tax revenues lagging badly, and dollar imports were at a lower level than desired owing to the port congestion. By raising the piaster take per dollar of imports, import absorption could be increased and the gap reduced accordingly. To the extent that the prices of imported goods theretofore had not been a matter of "windfall" profits, prices would rise under the initial impact of devaluation but this effect would be temporary and, hopefully, of limited extent.

The devaluation was announced on June 18, 1966. It changed the effective rate for most transactions from 60 to 118 piasters per dollar. This amounted to a piaster devaluation of 49 percent, but involved a 97 percent increase in the cost of foreign exchange. The accommodation rate for the

personal purchases of the U.S. troops which had been moved to 118 in September 1965, remained at that level. The rate for U.S. official purchases of piasters, which had been changed to 73.5:1 in June 1965 was moved only to 80:1. From that point until October 1967 when the official purchase rate was changed to 118:1, the U.S. government was thus receiving an unfavorable rate, resulting in additional dollar revenues to the GVN.

There were other measures taken at the same time as the June 18 devaluation:

1. Import licensing was freed from all restrictions and both the GVN and U.S. governments declared that large amounts of foreign exchange were available to meet demand.

2. Import licensing applications pending were all approved and penalties placed against withdrawing of applications.

3. The import industry itself, which had been closed to new entrants was opened, and more than 100 new firms were admitted over the next several months.

4. GVN civil and military personnel received a wage increase averaging about 27 percent.

5. A subsidy was placed on imported rice to hold its price at the pre-devaluation level; in effect, exempting it from devaluation.

6. Customs duties were not increased. They were recomputed to a base of 80:1 in such a way that the piaster amounts per dollar of imports were left unchanged. Because of this the average effective cost of imports (customs included) was about 70 percent as opposed to the 97 percent increase in the exchange cost alone.

9. Effects of the 1966 Devaluation

a. On inflation. The devaluation was successful in its primary goal of raising import absorption. An IMF study done at the time showed that in the absence of devaluation money supply would approximately have doubled in 1966 whereas in fact it rose by 37 percent.

On other counts the verdict is less clear cut. Prices rose by 33 percent from the end of May to the end of July, then stabilized and rose by only four percent from May to the end of the year. In early 1967 a new wave of inflation began and by August 1967 prices were 35 percent higher than a year earlier. This increase, in turn, compared with an increase in money supply during the twelve months from end-May 1966 to end-May 1967 of 17 percent.

From the foregoing events there is reason to believe that the psychological shock arising from the steepness of the devaluation was such as to dislodge hoarded cash, resulting in a price inflation considerably in excess of the monetary increase. Quite possibly the devaluation was too steep for a one time devaluation. The more appropriate judgment may be that it came too late; being too late it had to be steep.

b. On import licensing. One clearly unfavorable consequence of the measures was the surge of import licensing that ensued, a result of the action taken to free up the import trade. Total licensing in July, August, and September was \$246 million compared to \$133 million in the first quarter. Relaxation of import restrictions was needed to encourage competition in the import trade but coming as it did at a time of acute port congestion the effect was a worsening of that situation. By the end of July 1,000

barges in the Saigon river were being used as warehouses while the warehouses themselves were so jammed that goods could scarcely be located.

c. On foreign exchange reserves. The embarrassing rise in GVN foreign exchange reserves to \$300.7 million at the end of 1966 was attributable in part to the part tie-up and consequent inability of importers to utilize all of the foreign exchange available to them, but was helped along by the decision to peg the official purchase rate at 80:1 at the time of the devaluation. The situation was finally remedied in October 1967 when the rate was aligned with the remainder of the exchange rate structure at 118:1.

10. MACV Expenditure Control Program

The final anti-inflation measure to take place in 1966 was the implementation of the MACV expenditure control program. Both the personal expenditures of the troops and expenditures for salaries of local employees, rents, etc. had been rising sharply, and with the force level still expanding they were a matter of serious concern from an inflation standpoint. Of course, these same expenditures brought dollars to the GVN, and future economists in Viet Nam would look back with near disbelief to a time when a dollar inflow, for whatever purpose, was discouraged. In November, 1966, the U.S. Mission began setting expenditure ceilings, official and personal, agency by agency. Personal spending on the economy was discouraged by an extensive program including an advertising campaign to inform the G.I.s of the consequences of overspending ("Don't hurt them more"), high interest savings accounts, out of country R&R trips, and an expanded PX system. Through such devices, per capita spending of the troops was

-127

cut from a peak of \$30 a month to around \$10 a month in 1966. The program was to contribute greatly to the relative stability in 1967.

11. Inflation in 1967: the Rice Price

As mentioned above, there was a considerable surge of prices early in 1967, perhaps attributable to psychological factors stemming from the 1966 devaluation, but this had run its course by around mid-year. The port congestion had quite suddenly eased and goods were moving into commercial channels at last. The rate of inflation for the full year 1967 was 34 percent, but most of the increase occurred in the first half of the year. The increase in the fourth quarter was barely one percent. Apart from overall price movements, a development of particular interest took place in the price of rice.

Rice had been subsidized - not allowed to rise in price - at the time of the 1966 devaluation. In 1967 PL 480 Title I rice imports hit a record high 750,000 MT and the price of imported rice dominated the domestic rice market. This was a situation of which GVN officials generally approved, concerned as they were with the political implications of higher rice prices. U.S. planners, however, were increasingly concerned that the low price of domestic rice was adversely affecting farm incomes, the incentive to grow rice, and perhaps also the pacification program.

The issue was settled in March 1967 with a 20 to 25 piaster per kilo increase in the wholesale price of medium grain rice in Saigon. Contrary to some predictions, there were virtually no political repercussions.

B. Production and Incomes 1965-67

The large scale diversion of resources in support of the war effort

has already been discussed as one of the principal factors in the high level inflation of 1965-66. In this section we will take a closer look at the production changes involved and their impact in terms of individual incomes.

1. Domestic production

Agriculture was the sector hardest hit by the diversion of manpower resources to U.S. and GVN sector employment and this sector also suffered adverse effects from the widespread fighting. Industrial production gained throughout.

a. Rice. The 1966-67 crop year was the low point in rice production during the 1960s. Between 1964 and 1966 some 300,000 hectares of rice land went out of production and production itself declined by 800,000 MT of paddy. However, the hectarage under cultivation held steady during 1967 and production in the 1967-68 crop year rose by 350,000 MT (8 percent).

Though little remarked at the time, 1967 saw the start of the first pilot project to produce IR-8, the so called "miracle rice" that was before long to revolutionize rice farming in Viet Nam as in other developing countries.

b. Other agriculture. Most other agriculture crops did poorly during 1964-67. Reflecting developments in rice, the NIS index of agricultural production declined by 16.5 percent during 1964-66, then rose by 4.6 percent in 1967, the overall 1964-67 decline being one of 13 percent. Rubber production, heavily hit by the fighting and VC taxation and subject to an increasingly unfavorable exchange rate, declined by over 40 percent. Sugar production, a direct victim of the hostilities once cane fields were discovered to provide excellent cover for the Viet Cong, fell by 27 percent.

The one real success story in agriculture was vegetable production which, stimulated by U.S. troop demand, rose by 78 percent during this period.

Not included in the NIS agricultural index were pork, fish, and timber. Pork production, benefitting from the growing public demand for protein foods, rose during 1964-67 by five percent. The fish catch held its own and timber production declined by 27 percent.

c. Industry. Industrial production, almost unaffected by the fighting and benefitting directly from the import program, rose by 44 percent during 1964-67. Foodstuffs, beverages, and tobacco, which together accounted for 73 percent of the index weight, increased their combined production by 51 percent. Textile production rose only eight percent, its growth being hampered by imports of finished textiles from Far Eastern sources. Lesser industries doing better than average were: iron and steel, up 67 percent; electrical equipment, 210 percent; and plastic articles, 233 percent.

## 2. Goods Availablility

The increase in manufacturing production during 1964-67 was more than enough, in value terms, to offset the decline in agricultural output. Taking the indices for industrial and agricultural output above, production increased by about five percent. Douglas Dacy, in his study for the Institute of Defense Analysis, "Availability of Goods in South Viet Nam from 1964 Through 1967," took the matter a few steps further to obtain a concept of total goods availability. By factoring in certain production not included in the available indices, i.e. timber, pork, and fish, and adding imports not destined for the production process (generally speaking, consumer goods and P.L. 480 foodstuffs), he calculated that the

overall availability of goods rose during this period by some 21 percent.

Dacy's summary, by sector, is as follows:

	<u>Percent Increase in Goods Availability, 1964-67</u>
1. Agriculture (incl. pork, fish and timber)	3
2. Industry	45
3. Imports	<u>101</u>
Total	21

Of course, the influence of imports on goods availability was more than this summary alone would suggest, since the 45 percent increase in manufacturing production would not have been achieved without imported raw materials and capital goods.

### 3. National Accounts

The "goods availability" concept probably gives a more meaningful picture of the extent of national well-being than the national accounts, and not merely because of the notorious unreliability of Viet Nam's national account statistics. Yet the national accounts do need to be considered since they attempt, at least, to measure total production of goods and services, and they can indicate the magnitude of shifts in the factors of production.

Real gross national product is estimated to have risen by 12 percent during 1964-67. Net domestic product (GNP less depreciation and indirect taxes plus subsidies) rose by 16.3 percent. This figure has to be qualified right away by pointing out that the government sector accounted for 38 percent of the increase and that most of the government sector increase, in turn, consisted of wages and salaries paid to additional employees. To the extent the additional employees were military personnel, nothing was

126

added to the national wealth (one could make a case that nothing was added to the national wealth by adding civil servants either, but civil servants in theory at least provide services). Moreover, the government sector could be seen as even more significant if its contribution to the services sector could be determined. Withal, the private sector, net of government activity as near as it can be determined, is estimated by Dacy to have grown by 12.8 percent during 1964-67<sup>a/</sup>, a significant achievement under the circumstances.

As already suggested in the section on goods availability, such growth as occurred was largely attributable to imports, which by 1967 were equal to about 40 percent of GNP. The government sector, meanwhile, accounted for 23.7 percent of net domestic product, which compares with 21.3 percent in 1964, and a less developed country average for this indicator of about 13 percent. Neither indicator - the predominance of imports or of the government's share of the output of goods and services - was a good sign for the long-term health of the economy.

#### 4. Income Distribution

There is little question that as a general proposition people in 1967 were better off in terms of the material things of life than they were in 1964. It showed not merely in such economic indicators as those discussed above, but was obvious to most observers in terms of visible prosperity: i.e. motorbikes, TV sets, transistor radios, etc. The matter was not one of rapidly rising per capita income or consumption, because wage rates did not in fact rise by very much, but rather one of expanding employment. By 1967 virtually anyone who wanted to could find

a) Douglas Dacy, "The Wartime Economy of S. Vietnam."

a job. Many were moonlighting to hold two or more jobs, and families were listing more of their members with one or more jobs. Families, in effect, were pooling their incomes to obtain the goods that were increasingly visible to the observer.

Mission economists spent a good deal of effort in trying to determine which groups were benefiting most in the economic setting of the 1960's. Certain things were clear. Government employees fared poorly, at least from 1964 on, as public sector wages were held down in the effort to control inflation. According to one Mission study, real wages of GVN employees declined by from 52 to 55 percent, depending on job category and marital status, between the end of 1964 and the end of 1967. Certainly, then, they were not prospering (although, to be sure, they undoubtedly were among those moonlighting, therefore still able to afford some of the aforementioned luxuries).

The income split as between rural and urban dwellers, was less clear. Those gaining the most were the merchant classes, especially those in a position to take advantage of the "windfall" profits to be found in importing. The farmer, except for those directly affected by the hostilities, appears to have held his own during this period. Prosperity came to the urban dwellers first, but by 1967 the rural dwellers had probably caught up.

C. Imports, 1965-67

1. Volume of Imports

Imports roughly tripled in volume from 1964 to 1967 and came to account for about 40 percent of Viet Nam's GNP. The breakdown by category

of financing:

	Commercial Imports, 1964-67 (U.S.\$ Millions, Payments Basis)			
	<u>1964</u>	<u>1965</u>	<u>1966</u>	<u>1967</u>
GVN	94	85	237	288
(A.I.D. freight)*	(3)	(7)	(16)	(26)
CIP	105	155	259	194
P.L. 480	<u>34</u>	<u>48</u>	<u>76</u>	<u>153</u>
TOTAL	233	288	572	635

\* Payments for freight on A.I.D.-financed goods.

It should be noted that the data above cover commercial imports only, i.e. those paid for by private importers. The addition of imports under A.I.D.'s Project and PL 480 Title II (mainly relief shipments of foodstuffs) programs would bring the 1967 total close to \$800 million.<sup>a/</sup> In addition, probably \$100-200 million of goods entered the country illegally through one or another black market channel.

## 2. Composition of Imports; CIP

The composition of imports spanned a wide range from consumer goods through capital goods and raw materials. In general, the CIP provided capital goods and raw materials, while less essential goods were imported

<sup>a/</sup> It has been decided, for the purposes of this paper to consider imports in terms of commercial import payments only. The reason for this is twofold: (1) Data on import arrivals were extremely inaccurate. This inaccuracy applied both to the imports that were included under the payments concept - i.e. rice was never fully accounted for - and project assistance for which all data were guesstimates; (2) Commercial imports had the more significant economic impact. Since project imports were not paid for, they were not a factor in a monetary sense; they affected the economy in varying indirect ways.

with GVN exchange. The CIP, which is described in detail in a separate section, operated on the basis of a "Positive List" of goods eligible for financing under U.S. aid. Until 1971 the Positive List would be exclusive in the sense that goods listed thereon could be imported only through the CIP. An importer could, however, obtain a waiver to import with GVN-owned exchange in cases where he could not locate a U.S. supplier for a Positive List product. One effect of the Positive List technique was to increase the effective cost of the goods to the Vietnamese since the U.S., by and large, could not compete on price with other suppliers, notably those from Japan and Taiwan, especially when relative shipping costs were taken into account. This was to become an issue later on when sources of external financing began to be squeezed.

The big increase in consumer goods imports during this period is illustrated in part by the following: rice went from zero in 1964 to 750,000 tons (\$135.5 million) in 1967; fabric imports, from \$6.6 million to \$49.3 million; Motorcycles, from \$3.6 million to \$42.1 million; and POL (about half of which was properly considered a consumer import), from \$18.4 million to \$29 million. These figures underlay the prosperity that had begun to be evident by the end of 1967.

### 3. Implications of the Import Program

Of all the economic issues that analysts were to focus on in later years, probably none has generated more interest than the decision taken in 1964-65 to utilize imports as the principal anti-inflationary tool. The pros and cons of the debate are basically these:

Pro:

(1) Inflation had to be held under reasonable restraint. Given the delicate political climate of 1964-65, an inflation rate of Indonesian proportions, say several hundred percent a year, simply could not be afforded. And U.S. economists were quite convinced that an inflation of this magnitude was in store.

(2) The loss of production resulting from the transfer of resources to the war effort would have to be made up. Certainly this applied to the foodstuffs, especially rice, which would be readily available under PL 480, but also to basic production which would founder without large-scale raw material imports. Mass urban unemployment, as well as runaway inflation, had to be averted.

(3) There was no other way. The Vietnamese tax system, an archaic, poorly administered inheritance from the former French regime, simply could not be geared up to provide the tax revenues needed, even if drastically higher tax revenues were deemed feasible on political grounds. Moreover, the tax system was based to a large extent on imports. Of the domestic taxes, a predominant share were levied on a specific, rather than an ad valorem basis, so that they did not respond automatically to inflation.

Con:

(1) Taxes could have been raised. At least, the effort should have been made. In fact, the first meaningful effort to raise taxes was not made until 1966.

(2) The exchange rate could have been used to increase import absorption much earlier and more frequently than it was.

(3) The price paid for the result achieved - moderate success in controlling inflation - was too high in terms of:

a. Damage done to the country's basic economic structure.

There is no question that competition from competing imports - subsidized imports insofar as the piaster was overvalued - aborted development in many areas of both industry and agriculture, a point that came increasingly to be recognized in the 1970's. Export development was discouraged in so far as it had not already been completely discouraged by the overvalued exchange rate. But then, the high import policy itself encouraged an overvalued exchange rate.

b. Damage done to social and aesthetic sensibilities, and perhaps the fighting spirit of the South Vietnamese people, by the widespread presence of luxury goods in a poor country at war. The country's subsequent loss of support in the U.S. may have owed much to the quick impressions of the "Honda economy" gained by visiting journalists and Congressmen.

One might develop a middle-ground between these two positions. In retrospect, it does seem that there could have been more effort on taxes, and exchange rate policy throughout the 1960's does seem to have been laggard. Also, it can be argued that more inflation could have been incurred without bringing on disaster. However, hindsight is easy. It should be realized that on exchange rate policy, in particular, the GVN was extraordinarily resistant to pressures to devalue. Inflation was an overwhelming concern of economists and politicians alike. Most of all, no one thought the war would last ten years, let alone that we would lose it. The policy makers in 1964-65 were aware that they were inviting

economic distortions, but the extent of those distortions could hardly be perceived by people expecting a war of, at most, a few years' duration.

#### VII. The Tet Offensive

On February 1, 1968 the communists launched their Tet offensive, attacking across the country on a hitherto unprecedented scale. In this and the subsequent, lesser offensive of May-June 1968 they were to suffer appalling military reverses. However, the psychological impact of the attacks on the American public was to be decisive; in retrospect, the Tet offensive was to mark the beginning of the end of U.S. involvement.

##### A. Economic Impact

Economically, the Tet offensive was a costly setback, very nearly a disastrous one. Something over \$200 million in capital goods, including houses, were destroyed, and trade and commerce were halted for a number of weeks. Production of most urban goods and services was severely cut back. Industrial output for 1968 declined by nine percent, back to the 1966 level. Construction activity in the cities virtually halted. The agricultural sector suffered little in the way of permanent damage, but incurred significant near-term production declines. Fortunately, the 1967-68 rice harvest was largely in at the time the Tet attacks began, but the 1968-69 crop was to decline by seven percent. Agricultural output as a whole was off by eight percent. GNP is estimated to have declined by 4.5 percent, but the drop in private sector output must have been considerably more. Financially, increased military costs and the expense of caring for nearly a million new refugees placed an enormous additional strain on the GVN budget.

B. Mobilization and the Budget

A direct result of the Tet offensive was a full-scale mobilization by the GVN, which meant the drafting of another 300,000 men into the military. Only 100,000 of these were actually added to the payroll in 1968, but in combination with sharply higher costs of refugee care and other expenses associated with the upsurge in the level of fighting, this meant a VN\$ \*23.7 billion (25 percent) increase in government expenditures. Efforts were made to raise taxes. Austerity tax rates (on imports) were raised in April, and a 20 percent war surcharge was imposed on most domestic taxes in July. Yet, given the erosion in the tax base caused by the decline of economic activity, tax revenues for the year barely exceeded 1967. The result was a VN\$ 22.9 billion rise in the budget deficit for the year.

C. Monetary Gap and Inflation

The effect of the budget deficit on the overall monetary result for 1968 can be seen in the following Gap summary for 1967-67. Given the relative stability in the other factors, the increased deficit accounted for virtually all of the additional (over 1967) money supply increase in 1968.

Monetary Gap, 1967-68  
(VN\$ Billions)

	<u>1967</u>	<u>1968</u>
GVN Civil Budget	42.2	46.6
GVN Military Budget	55.3	74.6
Sub Total	97.5	121.2
U.S. Expenditures	46.8	47.7
Exports and Invisibles	12.0	9.6
Change in Bank Credit	-1.4	1.4
Total Expansionary	154.9	179.9

134

Monetary Gap, 1967-68  
(VN\$ Billions)

	<u>1967</u>	<u>1968</u>
GVN Revenues	53.2	54.0
Imports	73.7	66.3
Invisibles	8.6	10.6
Other	<u>0.7</u>	<u>7.3</u>
Total Contractionary	136.2	138.2
Errors and Omissions	- 0 -	0.2
Money Supply Increase (VN\$)	18.7	41.9
% Inc. in Money Supply	29%	51%
% Inc. in Consumer Prices	32%	23%

The surprising result, in monetary terms, was the very moderate degree of price inflation. Money supply rose by 51 percent, but prices rose only 23 percent from beginning to end of the year. This was due to the extraordinary mood of caution that gripped businessmen and households alike. In the uncertain climate of 1968, with people concerned for the safety of their money and possessions, the inclination was to hoard cash.

D. Balance of Payments and Exchange Reserves

Joining in the general business retrenchment of 1968, importers curtailed their activities. Import payments declined 14 percent below the 1967 level. Meanwhile, U.S. sector piaster purchases continued at a high level; a slump in troop spending was largely offset by rising official expenditures. As a result of these factors, official holdings of gold and foreign exchange continued to rise, reaching a peak of \$373 million in August and September, 1968.

The steady rise in foreign exchange reserves, from 1964 to 1968, ended at that point. It seems as good a point as any to bring the balance of payments up to date.

Simplified Balance of Payments, 1964-68  
(U.S.\$ Millions)

	<u>1964</u>	<u>1965</u>	<u>1966</u>	<u>1967</u>	<u>1968</u>
<b>A. <u>Balance of Trade</u></b>					
1. Exports	49	40	25	22	16
2. Commercial Imports, c.i.t.	<u>-233</u>	<u>-288</u>	<u>-572</u>	<u>-635</u>	<u>-548</u>
Balance of Trade	-184	-248	-547	-613	-532
<b>B. <u>U.S. Support</u></b>					
1. U.S. Aid	139	203	335	347	239
(CIP)	(105)	(155)	(259)	(194)	(101)
(PL 480 Title I)	( 34)	( 48)	( 76)	(153)	(138)
2. U.S. Piaster Purchases	15	126	333	327	301
(Official)	( 8)	( 94)	(233)	(212)	(246)
(Personal)	( 7)	( 32)	(100)	(115)	( 55)
Total U.S. Support	154	329	668	674	550
<b>C. Net Invisibles and Other</b>	-11	-41	+17	-46	-3
<b>D. Change in GVN Reserves     From Operations</b>	-41	+40	+138	+15	+15

VIII. Recovery From the Tet Offensive, 1968

By mid-summer of 1968 much of the damage done in the Tet and May-June offensives had been restored. Those made homeless, numbering nearly a million, had been housed, many in structures built by the people themselves with the help of USAID contributions of cement and roofing, and the GVN's contributions of cash. Industry, which had suffered damages to plant and equipment estimated at \$50 million, had begun to recover with the help of

a \$10 million Reconstruction Loan from USAID. The principal land and waterways were reopened, major power systems were put back into operation, and pacification teams moved back into the rural areas. Most of all, from the point of view of economic recovery, it was clear that the Viet Cong had failed in their all-out bid for control. Investors and speculators alike could take heart.

A. The Surge in Import Activity

One of the first signs of business recovery was a surge of new license applications by importers. Total import licensing rose from \$170.5 million in the third quarter to an unprecedented \$225 million in the fourth quarter of 1968. By contrast, in 1967, a good year for business, licensing had averaged \$132 million per quarter. The import boom was to last until May, 1969 when the GVN, alarmed by its declining exchange reserves, would put on the brakes. The heavy import demand of this period is generally attributed to a depletion of inventories during 1967 and through the Tet offensive. This is mainly surmise because no one in Viet Nam ever had a good notion of what inventories were. Perhaps more important, the exchange rate, still at 118:1, was once again getting out of line. Imports were becoming cheap relative to domestic goods.

As to the measurement of inventories, USAID attempted to keep track of CIP goods held in bank warehouses, but this was less than half the story, and never a very accurate one at that. USAID also tried to urge/compel the Vietnamese banking system to establish a computerized Import Credit Data System that would track all goods from time of ordering to disposal in the marketplace, but this very costly effort finally succumbed in 1969 under the weight of GVN apathy.

B. Agricultural Activity

The agricultural economy began its recovery sometime after mid-year; the precise timing is not clear. At any rate, the declines in production noted in Section VII should be read with this in mind: that it was not all a down year.

A significant development in 1968 was the planting of 100,000 hectares to IR-8 seed, or Miracle rice. IR-8 yielded up to five metric tons of rice per hectare, as compared with the roughly two MT per hectare yielded by the traditional varieties.

Also, in November the wholesale rice price was raised by 25 percent, sufficient once again to remove the subsidy on imported rice.

IX. End of The Old Ways; January 1969 - August 1970

This Section covers a period beginning with the outset of 1969 and ending with the first of the major reform measures in the fall of 1970. It was a period of improving security and relative prosperity but one in which a growing inflationary threat combined with the prospect of declining aid levels would lead finally to new policy approaches.

A. Agricultural Prosperity

The years 1969 and 1970 were good ones for the farmer generally, and rice farmers in particular. Rice production rose by 700,000 MT in 1969 and another 400,000 MT in 1970. At 5.5 million MT in 1970, rice output had surpassed the 1964 level and was at the highest level achieved since the Second World War. Apart from increased plantings to miracle rice, rice output was benefitting from a greater application of fertilizer, and from increased use of tractors and water pumps. The "green revolution"

had arrived in Viet Nam.

Prices of agricultural inputs did not keep up with farm product prices during this period, partly because of the fixed exchange rate. The per kilo prices of rice and fertilizer, for instance, which were in a ratio of 1 to 1 in 1967, were in a ratio of 2.5 to 1 by mid-1970. Moreover, paddy prices had moved ahead of the cost-of-living after 1968:

	<u>Average Paddy Price in Middle Delta</u>	<u>Cost of Living Lower Class - NIS</u>
1967	100	100
1968	95	117
1969	181	141
1970	209	182

There was no question that the Delta rice farmer's terms of trade were improving in this period.

#### B. Industry

Industrial output rebounded strongly in 1969, rising 24 percent from the depressed level of the Tet offensive. Nevertheless, industry was accorded a relatively low priority during this period. With high level inflation the predominant concern (see below), USAID was inclined to discourage investment projects that could not ensure a quick payoff in terms of output. One example of the overriding concern with stabilization was the temporary suspension of the so-called "Commercial Consumables" program. Vietnamese industry had begun, gradually, to supply some of the goods required by the Vietnamese armed forces - such as boots, barbed wire, canteens, etc. - thereby reducing the cost of the Military Assistance Support Finding (MASF) program. In late 1969, the USAID Joint Economic

Office effected a suspension of the "Commercial Consumables" program on the ground that with overfull employment and high level inflation these goods were best supplied from outside the country, at least for the time being. The program was reinstated in 1971 as the "Local Procurement Program".

C. Import Licensing and Reserve Drain

The heavy import licensing that had begun in the summer of 1968 continued unabated into 1969. Total licensing in the first quarter was \$190 million, compared with \$225 million in the fourth quarter of 1968. Since the first quarter is normally a seasonal low point for import activity, the slight reduction could be regarded as not significant. Reflecting the trend, official exchange reserves continued the decline begun in September 1968 when they had peaked at \$373 million. In May, with reserves down to \$282 million, the government began to ration foreign exchange for imports (N.B.: automobiles and motorbikes had already been banned, in January). The reserve decline was to continue until a temporary low point of \$204 million was reached at the end of June 1969. Import licensing, meanwhile, fell to \$155 million in the second and third quarters, respectively.

D. Growing Inflationary Threat

The eight-month period from August, 1968 to April, 1969 was one of remarkable stability in terms of the price indices. The NIS consumer price index rose only 3.5 percent during that period. However, every economist in Viet Nam knew that it could not last. The principal factor in the stability of prices was the heavy volume of imports, which from September 1968 to June 1969 resulted in a decline in exchange reserves

140

of \$169 million. This plainly could not go on; indeed, the government acted in May to halt the hemorrhage by the simple expedient of letting import license applications pile up on the desks of Ministry of Economy officials. The slowdown in licensing in May foretold lower import levels by mid-summer.

Other factors were at work, of both a long and short-term nature, pointing to increasing inflationary pressures.

For the longer-term, there was the U.S. force withdrawal, which began in the winter of 1969. U.S. forces reached their peak level of 542,000 in January and would be down to 474,000 by the end of 1969. In the wake of the Tet offensive grumblings had begun in the Congress about aid to Viet Nam, and no one could be sure anymore that the aid requirement would be fully met. The U.S. force withdrawal, then, loomed as a growing economic, as well as a military threat, since the troops would be taking their dollars with them (by now, of course, the U.S. presence had come to be recognized - by economists, if not the local press - as a deflationary factor, since the imports and import taxes financed by U.S. piaster purchases more than offset the initial inflationary effect of U.S. piaster spending). To be sure, it would be, for a combination of reasons, another two years before the U.S. withdrawal was to mean reduced dollar earnings from the U.S. presence, but this was not apparent at the at the time.

With the U.S. forces withdrawing, the GVN felt it had no option, but to increase its own force level. Vietnamization was formally proclaimed at the Midway Conference in June, and the decision was thereupon taken to

raise the force level to 1,100,000 men, an increase of some 250,000 from the 1969 force level.

Given the manpower situation at the time, the new troops would have to come largely from the economy. The force level had already been increased by 150,000 in 1969, and the employment situation could by now be described as overfull. Normal population growth could supply only about 50,000 draft-age males a year.

On the budgetary front, a long-delayed pay increase was decreed. It would provide a flat 1,000 piaster per month pay increase for all GVN employees, for a total cost of 14 billion piasters annually. While the pay increase was effective July 1 the GVN delayed its impact by holding back the first disbursement until September.

Another, altogether new factor in the budgetary outlook, was the Land Reform program, which had been announced by President Thieu in his New Year's address on January 1, 1969. The program, to begin in 1970, would result eventually in the transfer of over one million hectares of farm land to their tenants. The former landlords were to be paid 20 percent in cash and 80 percent in ten-year six percent bonds. The cost to the GVN budget would be VN\$ 10 billion by 1971, rising to VN\$ 22 billion in 1974.

#### E. Anti-Inflation Efforts, Early 1969

The GVN's initial anti-inflation effort came in February with the imposition of a new "special perequation tax" and a reform of the tariff structure. A more significant move took place in June when perequation tax rates were raised and extended for the first time to CIP imports.

142

The net addition to 1969 revenues was VN\$ 8-9 billion, a not inconsiderable amount, but well short of the cost of the pay increase alone.

By September it was apparent that in the absence of drastic action, the result would be a 1970 monetary gap on the order of VN\$ 80 to VN\$ 90 billion; i.e. a money supply increase on the order of 60 percent.

F. The Failure To Devalue

The reader may wonder why there was no devaluation at this time. Devaluation seemed indicated on several counts: no devaluation having occurred since 1966, imports had once again become overly cheap relative to domestic goods; devaluation was the surest and cleanest way to increase import absorption and cut the monetary gap; and in the absence of devaluation, the increasingly unrealistic valuation of the piaster was being reflected in rising black market activity. The black market rate for a \$10 bill rose from 200 piasters at the end of 1968 to 225 in September and would soar to 360 by year-end.

The answer to the question is that the GVN would not have it. It is not that the U.S. advisors did not try to persuade them to devalue; indeed, scarcely a meeting between GVN and USAID economic officials passed without the subject being debated. The GVN was told that the increasingly unfavorable accommodation rate, especially, was getting bad notices in the U.S. and that Congressmen were expressing interest in the fact that, at 118:1, the G.I. was being asked to give foreign aid to Viet Nam.

Appeals to self-interest were tried. The overvalued piaster was causing capital flight, notably through the practice of over invoicing

imports. The G.I.'s were buying less and less of their piaster requirements through legal channels. By mid-1969 the average G.I. was spending \$7 per month with piasters purchased legally, versus \$30 in 1965. Obviously, he was going to the black market. Finally, the very spectacle of a rising black market rate and of Saigon market places choked with black market goods was becoming more and more of a turn-off to reporters and visiting Congressmen increasingly inclined to question the war anyway.

All to no avail. As to G.I. spending, GVN officials firmly believed that a devaluation would not help (as events were later to show they could not have been more wrong). They argued insistently that as long as there was any black market premium at all the G.I.'s who had by now established their black market channels, would continue to buy their piasters illegally, and there would always be a black market premium, so the argument went, because with continuing inflation, any fixed official rate would soon be out of line. The "crawling peg" was barely considered at the time.

GVN officials were, of course, concerned about the political consequences of a devaluation. However, uppermost in their minds, if seldom mentioned to U.S. officials, was the fact that the GVN stood to realize a higher level of dollar inflow from U.S. official piaster purchases the lower the rate of exchange. Piaster purchases for official purposes were not aid, insofar as the official rate was at a realistic level, because the U.S. sector consumed Vietnamese resources. But to the extent the U.S. paid more for their piasters than they were worth, they were providing a form of grant aid. This "hidden aid," little noticed by the Congress at the time, could never be precisely measured, any more than the "true" value of the piaster could be measured, but it was certainly over \$200

744

million in 1969.

Unable to move the GVN on the devaluation issue, and unable or unwilling to try to force them to it, the U.S. advisors agreed to an alternative solution.

G. Austerity Tax Measure of October 1969

Aided by the government's success in delaying required expenditures, notably the pay increase which had been approved in July, the money supply remained relatively stable, rising only six percent during January - August, 1969. However, perhaps in anticipation of what was to come, prices had begun to move upward again in May. Between April and October consumer prices rose at an annual rate of 49 percent.

In September an IMF Mission arrived to work on a new tax package along with U.S. and GVN economic officials. The result, the so-called "Austerity Tax Measure", was announced on October 28, 1969. Austerity taxes, which were one of three schedules of GVN import taxes, were increased by amounts ranging from VN\$ 20 to VN\$ 520 per dollar on items comprising over two-thirds of Viet Nam's total imports. The tax increases were assessed according to a number of criteria, foremost of which was the degree of "essentiality" of the product. The effect of the tax, taking account of the exchange rate itself and Viet Nam's two other varieties of import tax (customs tax and perequation tax)--which were not altered by the decree--was to raise the effective cost of imported goods by an average 49%. About one-third of the country's imports were exempted entirely; considering only the two-thirds that were taxed, the average increase in effective import cost was an estimated 64%. Given an effective collection

-145-

performance at the Customs, the measure could have resulted in a revenue increase of over \$VN 40 billion in 1970. In the final event the measure raised about VN\$ 27 billion, but even this brought import revenues to a level 60 percent over those that would have been raised in its absence.

While the measure was labelled an "austerity" tax and was, in fact, concentrated most heavily on luxury items, it proved necessary for revenue purposes to raise tax rates on numerous borderline items, some of them of importance either as foodstuffs or as raw materials for agriculture and industry. Thus, for example, wheat flour was taxed an additional VN\$ 40 for a 22 percent increase in the effective import cost; Portland cement, VN\$ 40 (28 percent increase in cost); metal sheets, VN\$ 120 (81 percent increase in cost); and small marine engines, an item of crucial importance in agriculture and fishing, VN\$ 80 (53 percent increase in cost).

#### H. Reaction To The Measure

The immediate reaction to the measure was a country-wide wave of price increases, many of them not justifiable on economic grounds, and considerable protest from the public and the legislature. By November 13, 1969, two weeks after the measure, the USAID price index was up 12 percent over its pre-decree level. Unfortunately, speculation on rice was at its height at this juncture, adding fuel to the fire. Rice prices in the same two weeks rose over 20 percent; even so, the portion of the overall price increase attributable to the measure alone was as much as ten percent.

Prices began to fall back slightly later in November as the purport of the measure began to be understood--but the protest continued in the legislature. On November 14 the GVN issued a decree rescinding a portion

of the tax hikes, notably those on petroleum products. The amount of the rollback, in revenue terms, was only about VN\$ 3 billion, but it was sufficient to appease much, though not all, of the legislative opposition.

I. Inflation and Speculation in 1970

To the disappointment of the economic officials, prices soon resumed their upward march. Between January 1 and July 30 consumer prices rose by about 25 percent. The increase could not be attributed to monetary factors, as the money supply during this period rose by only eight percent. Rather, it seemed to relate to the sheer duration of the inflation preceding. The faith of most Vietnamese in their money was finally crumbling. The realization that piaster notes were not a secure form of saving had penetrated all levels of the population. Speculation was intense in imported goods, gold, green dollars, real estate--anything that promised to hold its value. It was also apparent in the activity in two important sectors of the economy, the rice market and the import community.

1. The Rice Market

Indicative of the speculative climate that had taken hold in 1970 was the behavior of the rice market. As noted earlier, the 1969-70 rice crop was a good one, some 700,000 tons higher than the preceding year. Based on this, one would have expected an increased flow of local rice to market, a declining demand for imports, and rather soft prices. Instead, local rice marketing was at only about the previous year's rate, consumption of imports reached nearly 500,000 tons in 1970, about the same as 1969, and prices, which rose sharply in late 1969, remained high and steady throughout 1970. Import stocks, which were only 48,000 tons

- 117 -

at the beginning of 1970, remained at low levels for most of first-half 1970. It appeared that several hundred thousand tons of paddy rice were withheld from the market by farmers, merchants and speculators and apparent rice consumption in urban areas was high.

2. Import Activity

Speculation was also evident in the market for imported goods generally. A wave of heavy import licensing, which began in October 1969, after passage of the austerity tax decree, was only brought down to a low level after February, when the GVN licensing authorities, concerned by the prospect of declining reserves, once again sharply restricted licensing. After February 1970, the list of goods eligible for licensing was confined to necessities, with even such items as spare parts for machinery excluded, and the licensing average was only about \$20 million a month. CIP licensing was also subjected to a number of restrictions. During FY 1970, about 40 percent of the license applications submitted to the USAID were rejected, usually because, in the judgment of USAID CIP staff, applications included demand above current consumption. One result of both GVN and CIP restrictions was to raise market prices of most imported products considerably above their import cost. The excess, as was the case in 1966, was a windfall profit, which accrued to the importer and to any others with whom he was obliged to split it. The windfall gains were greatest for GVN-financed goods, but were also substantial on some CIP commodities.

J. Verdict on the Austerity Tax; Skulduggery at the Customs

For the most part, the Austerity Tax Measure did what it was intended

- 148 -

to do. It raised import revenues by about VN\$ 27 billion which, in turn, meant roughly a 55 percent reduction in the potential money supply increase for 1969. But that is probably about all that can be said for it. In the longer-run, it could be faulted even as a revenue measure for the simple reason that, as an import tax measure, it tended to perpetuate the country's dependence on imports.

For the short-term, the measure, together with the near-hysterical public and press reaction to it, seemed to exacerbate the various speculative forces at work. Perhaps the public, and the import community, realized that the Austerity Tax Measure was not the answer to Viet Nam's longer-term inflation problem, and were reacting in the certainty of more to come.

An interesting result of the measure was the opportunities, and incentives, it gave to importers and dishonest customs officials to connive at falsifying invoices to effect capital flight. The opportunities because of the great number of new tariff categories created; the incentive because of the greater cost to the importer of not getting his product moved into a lower category. After the Tax Measure had been in effect for several months, a USAID study based on a comparison of the actual and theoretical tax take showed that import revenues were considerably less than they should have been. The matter was brought to the attention of the Ministry of Finance and resulted eventually in the firing of the Customs Chief and most of his team.

K. Gap Results, 1969-70

Anticipating in part Section X which will deal with the situation from the time of the first monetary reform in August, 1970, the

Monetary Gap results for 1968-70 are summarized below:

	Monetary Gap, 1968-70 (VN\$ Billions)		
	<u>1968</u>	<u>1969</u>	<u>1970</u>
<u>Expansionary</u>			
GVN Expenditures	121	133	187
(of which: military)	( 75)	( 92)	(122)
U.S. Expenditures	48	56	53
Exports and Invisibles	10	12	12
Credit Expansion	<u>1</u>	<u>4</u>	<u>15</u>
Sub Total	180	205	267
<u>Contractionary</u>			
Imports	66	82	82
Revenues	54	87	123
(Domestic)	(28)	(36)	(52)
(Import)	(26)	(51)	(71)
Invisible Imports	11	11	11
Savings, etc.	<u>7</u>	<u>11</u>	<u>27</u>
Sub Total	138	191	243
Errors and Omissions	- 0 -	3	-2
Gap (Inc. in Money Supply):			
VN\$	42	17	22
Percentage	51%	13%	16%
% Inc. in Prices (NIS)	23%	31%	32%

As can be seen, the increase in money supply in 1970 was held to VN\$ 22 billion, or 16 percent. In the absence of the Austerity Tax Measure,

60

the money supply increase would have been about VN\$ 49 billion<sup>a/</sup> or 35 percent.

By August 1970 the latest surge of inflation appeared to have run its course. The NIS consumer price index rose only 6.5 percent from August to the year-end. The explanation for the levelling off in prices seems to lie in the decline in liquidity. In the sixteen months from April 1969 to August 1970 prices had risen 59 percent, but money supply only 22 percent. Bank credit was in short supply and finally, the Austerity Tax Measure, as inefficient as it may have been had raised the cost of imports considerably, thereby putting an additional element of squeeze on importers. The respite in the inflation was not readily seen as such at the time, but in retrospect it was an excellent time for the set of reform measures that were to follow.

a/ The 1969-70 Gap comparison shows an increase in import revenues of VN\$ 20 billion. The difference between this figure and the VN\$ 27 billion by which it has been said that the Austerity Tax Measure raised import revenues is explained by the lower volume of GVN imports - which account for the bulk of import revenues - in 1970; GVN imports were \$403 million in 1969 and \$360 million in 1970.

X. Economic Reform and Progress, September 1970 - March 1972

This section covers a period from the start of the 1970-71 economic reforms to the communists' Easter offensive of April 1972. It was probably the best year and a half for Viet Nam of the U.S. involvement, certainly the best since the 1950's.

A. A Change in Economic Leadership

In October 1969 Pham Kim Ngoc, an American-educated businessman of liberal economic persuasion, became Minister of Economy. Ngoc had his baptism of fire in the travail of the Austerity Tax Measure (for which he probably cannot be blamed; the measure was adopted too soon after Ngoc assumed office for him to have a hand in its design). During 1970 he became the informal leader of a group of young, like-minded, mostly American-educated economists, including soon-to-be Minister of Finance Ha Yuan Trung, who shared in common two traits worth noting: a conviction that the operations of the economy are best left to the free play of the market place, and a willingness to take unpopular decisions in the face of public opinion. Ngoc and Trung would engineer the highly successful reforms of 1970-71. Their tenure would span the best year of the U.S. involvement (1971) and one of the worst (1972) before both would lose office in the midst of a deteriorating situation in October 1973.

B. Interest Rate Reform of September 1970

(1) Background

Until August 1970 interest rate policy - or the lack of it - had been dictated by the needs of the import community, which accounted for 85 to 90 percent of the business of the Saigon banks. Importers wanted

low interest rates in order to facilitate their activities, in particular the carrying of large stocks over frequently long periods of time. Lending rates ranged from 9 to 13 percent and savings rates from 8 to 12 percent, depending on terms. Under the circumstances, with inflation averaging 25 to 50 percent, savings of individuals and businesses were minimal. For example, during the 18-month period from January 1, 1969 to June 30, 1970, a "normal" period in terms of inflation in Viet Nam, savings and time deposits of the commercial banks rose by VN\$7.9 billion. Another VN\$1.1 billion went into private sector holdings of Treasury bills, bringing the combined increase in bank/bill savings to VN\$9 billion. The money supply, meanwhile, increased by VN\$24.9 billion. Thus, bank savings during this period amounted to only 26.5 percent of the combined money supply and savings increase ( $\frac{9}{9 + 24.9} = .265$ ). A ratio close to 50 percent was thought both desirable and attainable.

On their part, the banks were not interested in attempting to encourage savings deposits. Apart from sheer inertia (which in their case was always considerable), the reasons seemed to be that: (1) operations were profitable as things were; (2) they would not be able to find suitable lending outlets for such funds as they could attract; and (3) it wouldn't work anyway. The kind of interest rates needed to really attract savings in Viet Nam would be so high, the argument went, as to provoke an instant crisis in business - mostly import-circles.

Against these arguments was the incontestable economic case to the effect that savings were essential, both on anti-inflation grounds and to provide a basis for economic development. Inflation would be curbed both by drawing funds out of circulation, and by making more costly - thereby

discouraging - the widespread speculation on inventories that had been taking place.

(2) Measure of September 1970

The September decree on interest rates resulted in an approximate doubling of the pre-existing rate schedule. The new lending rates were set at from 18 to 24 percent; savings and time deposit rates at from 10 to 21 percent (although one popular form of saving, a savings deposit with lottery feature, paid only 8 percent). Treasury Bill rates were increased in line with savings rates. Simultaneously with the increase in interest rates, the GVN imposed a system of advance deposits on imports by which importers of most GVN-financed goods were required to post deposits at the time of application for an import license. This was an additional anti-speculation measure that would prevent new importers from holding an advantage over those with old stocks on hand.

(3) Aftermath of the Measure

While it could be argued that savings rates were still negative, nevertheless, savings and time deposits of the private sector turned upward immediately in response to the measure. The increase amounted to VN\$6 billion during the fourth quarter of 1970, and another VN\$27.4 billion in 1971. Adding Treasury bill holdings of the private sector, the 1971 savings increase came to VN\$31.3 billion. The 1971 increase compared with a money supply increase of VN\$35.9 billion for that year. Thus,  $\frac{31.3}{35.9} = .47$  percent of the potential money supply increase (31.3 + 35.9 = .47) was siphoned into savings deposits. In subsequent years this ratio would rise to over 60 percent.

The Interest Rate Reform was also successful in its other aim of

-157-

discouraging speculation. While inventory data were never available to confirm the point, observers generally agreed that the measure had resulted in the disgorging of a considerable volume of goods being held for speculative purposes. At any rate, price inflation, which had begun to slow by July, remained at a moderate 20 percent annual rate through the end of 1970. The relative calm on the inflation front prevailed despite the partial devaluation of October 3.

C. Measures of October 3, 1970

The Economic and Financial Measures of October 3, 1970 comprised the following:

(1) Establishment of a new "parallel rate" market, at VN\$275: U.S.\$1, to apply to:

- Accommodation purchases of the troops;
- All other financial transactions, except those of the government and student remittances;
- Exports
- Certain GVN imports, mostly in the "less essential" category, estimated to account for about half of all GVN imports.

(2) Increases in perequation tax rates of up to 140 piasters per dollar on a range of mostly GVN-financed imports. Three USAID-financed products - fish nets, yarn for fish nets, and fishing boats - were included. These tax increases were mainly for protective purposes.

(3) A pay increase for civil servants and military personnel, estimated as averaging 17 percent on total compensation, and an increase in veterans' allowances.

(4) Elimination of the rice price differential between Central

155-

Viet Nam and the rest of the country.

(5) A VN\$10 piaster (30 percent) increase in the wholesale price of sugar

D. Effect of the October Measures

The September and October measures were the first of a series of actions that were to take place in 1970-71, culminating in the major reform package of November 15, 1971. Taken together, their aim would be to increase the effectiveness of the market economy while moving the country in the direction of self-sufficiency. Most of the policy areas to be covered were touched upon in October 1970, notably exchange rate reform, export promotion, discouragement of less essential imports, and elimination of import subsidies. Two near-term effects of this set of measures may be noted here:

(1) Degree of Devaluation

Establishment of the parallel rate, together with the accompanying increases in perequation tax amounted to a de facto devaluation estimated by the Mission at 15 percent. A further round of perequation tax increases on December 12 added another five percent to average effective import costs.

(2) Accommodation Rate

The increase in the accommodation rate to 275:1 had a dramatic and immediate effect. Per capita expenditures of the troops rose from a monthly average of \$4 before the measure to \$22 after. Per capita monthly expenditures of DOD contractor personnel rose from \$46 to \$247. The increases came despite the fact that, even at 275:1, the accommodation rate still was far behind the Saigon black market rate of around

400:1.<sup>a/</sup> And in fact, per capita expenditure rates were to climb much higher following the devaluation of November 1971: to \$50 a month for the troops, \$448 a month for DOD contractors.

E. Reform Measures of 1971

It is likely that 1971 will be remembered more for its economic policy reforms than for any other feature of the economic scene. Before assessing the principal economic developments of that year, the nature and timing of these measures will be set down here. Note that only the most significant are listed in this paper. The measures in question, following on those undertaken in September-October 1970, took place in March, June, August and November of 1971, as follows:

March 6, 1971

- Import taxes on sugar and wheat flour were raised, so that prices of sugar nearly doubled and of flour were raised by 30 percent.
- The price of imported rice was raised from VN\$31/kg to VN\$41.5kg (for medium grain). Rice rationing in Central Viet Nam was abolished.
- GVN employees were granted an increase in the cost of living allowance to raise total compensation an average of about four percent.
- Freight and insurance on GVN-financed and PL 480 imports were shifted to the 275 rate.
- It was agreed that GVN-owned companies would henceforth go to the commercial banks for credit, rather than to the Treasury.

June 7, 1971

- A new "general licensing" system (GL) was introduced for imports. At 400 piasters per dollar, the GL was made mandatory for parallel market goods and optional for 118 rate goods.
- A new export rate of 350 was created (275 + 75 subsidy).

---

<sup>a/</sup> Black market rates peaked in October. The rate for \$10 green reached 435:1 in that month, then declined to 388:1 at the year-end.

157-

August 1971

- Taxes and prices of cigarettes were raised.
- For the first time, dual licensing (CIP and GVN) was instituted on a limited list of capital equipment items and spare parts, with differential rates of 118 and 400 on U.S. and GVN-financed imports, respectively.

November 15, 1971

- The exchange rate structure was revised, so that four principal rates were left:
  - 118 - still the rate for official foreign government purchases, and also for GVN transactions and remittances to students abroad
  - 275 - for U.S.-financed imports
  - 400 - for GVN-financed imports
  - 410 - for invisibles generally, personal accommodations, transactions on capital account, and for exports

The last three rates above were referred to as the parallel market rates, categories I, II, III, respectively. (Informally, they became known more generally as the A.I.D. rate, the GVN rate, and the Financial Rate).

- The decision was made by the GVN that the three parallel market rates would be adjusted frequently by small steps, on decision by a committee composed of the Ministers of Finance and Economy and the Governor of the National Bank.
- GVN imports were placed under the GL system, and import-licensing was, in principle at least, done away with except for U.S.-financed imports.
- Import taxes were completely revised. The old schedules of perequation tax, import duty, and austerity tax were abolished and replaced by a single schedule of four rates: 0, 25, 50 and 200 percent. Raw materials and other basic commodities took the 0 rate, most manufactured goods the 25 rate, luxuries the 50 rate, and the 200 rate was reserved for personal-use vehicles. In addition, the Ministry of Economy announced its willingness to grant a perequation tax for protective purposes on request by local industry. Generally the rate would be 25 percent.
- The GVN selling price of both domestic and imported rice in Central Viet Nam was raised to substantially eliminate the subsidy

- on it.

- GVN wages were raised as follows: a general increase of 1,200 piasters per month was given to all employees; soldiers in RVNAF combat infantry battalions received a special allowance of 4,500 piasters per month; soldiers in RF mobile battalions received a similar allowance of 3,500 piasters per month. Special allowances for National Police and for tax and customs collectors were decided upon for later implementation.

In the face of pleas from the private sector, it was decided that machinery and equipment being imported under CIP for approved investment projects, ordered before the November 15 reform but not delivered, would be admitted at the old rate of 118. Also, it was decided exceptionally to grant a protective perequisition tax higher than 25 percent for textiles. The initial rate was set at 50 percent and, while the intention was to reduce it by mid-1972, the reduction was not, in fact, to take place.

#### Additional Measures Taken in Early 1972

The GVN took a number of additional measures during the first quarter of 1972, mostly intended to tidy up details of the November reform:

- The prices of gasoline and kerosene were raised so as to roughly eliminate the subsidies involved. Premium gasoline went from 21 to 30 piasters/liter, kerosene from 11 to 16 piasters/liter.
- On March 1, the National Economic Development Fund was launched with a VN\$10 billion piaster initial commitment of counterpart funds.
- The exchange rate for fertilizer and pesticides was raised from 118 to 200.
- Prices of water and electricity were raised.
- On April 1, the exchange rate for official purchase of piasters by foreign government was raised from 118 to the category III parallel rate, then 410.

#### F. Exchange Rate Considerations

A major share of the 1970-71 reforms had to do with the exchange

rate-tariff structure; not merely the level of import costs, but also the tariff structure, the GVN-CIP exchange rate differential, and the GVN licensing system.

(1) Devaluation and Tariff Simplification

The exchange rate-tariff reforms involved both devaluation and tariff simplification. The tax measures of March 5, the progressive adoption of Open General Licensing at the 400:1 rate beginning in June, and the November 15 reforms, taken together, provided a devaluation of some 33 percent (Mission estimate). After November 15, it could be said that the piaster was at, or very near, a realistic level vis-a-vis other currencies.

The tariff revision of November 15 changed the import tax structure overnight from one of three schedules, each with scores of rates, to two extremely simple schedules: a customs tariff with four rates: 0, 25, 50, and 200 percent; and a perequation tax with two rates for limited, protective purposes. The job of the Customs authorities would be simplified at the same time that their opportunities for false classification would be limited.

Not only was the import tax structure drastically simplified, it was also sharply lowered. The result was to shift much of the collection of import revenues to the exchange rate, where it could be more effectively administered. The GVN had come full circle from the Austerity Tax Measure of October 1969.

(2) GVN-CIP Rate Differential

With the adoption of the parallel rate of 275:1 in October 1970, the GVN was, in part, recognizing through its exchange rate policy the higher

160

cost of GVN-financed relative to CIP goods (not entirely, because there was also an intention to discourage importation of those goods placed in the parallel rate market). The process was extended with the adoption of Open General Licensing in June 1971, wherein more and more GVN-financed goods became subject to the 400:1 rate. With the November 15, 1971 move, all GVN goods were at 400:1 and all CIP goods at 275:1. These were not, of course, the effective import costs, since import tariffs were added; with import tariffs included, the differential was more than that suggested by the 400 to 275 spread.

There was nothing scientific about the selection of the 400 and 275 rates; the spread was, at any rate, to shift repeatedly throughout the remaining period of U.S. involvement. Economists did know that CIP goods were considerably more expensive than the comparable GVN-financed product from Japan or Taiwan - for reasons of higher costs of shipping, red tape, etc., as well as product price - but they did not know how much more. They were anxious to get the exchange rate spread as "right" as possible to prevent unsettling swings in importer activity from one list to the other, and meanwhile they worried about the real economic cost of tied aid (i.e. CIP). They believed that this cost was so high as to offset the balance of payments saving ostensibly gained through tied aid, and argued that by untying aid, the savings in real import costs would enable a reduction in the overall aid level without any real cost to Viet Nam. These considerations led to the experiment with dual licensing in June 1971

(3) Dual Licensing

The Mission's case with respect to the economic cost of tied aid

could not be statistically proven, but in hopes of demonstrating their point, Mission economists persuaded the GVN and AID/Washington to have certain machinery imports (in which the U.S. was thought to have as much of a competitive advantage as anywhere) available under both GVN and CIP financing for a trial period. If importers showed a demonstrable preference for the GVN-financed product at 400:1, as opposed to the CIP product at 118:1, this would constitute a solid argument in favor of untying foreign aid - or at least a large portion of it.

The result of the experiment was inconclusive. While machinery licensing was about evenly split as between GVN and CIP during the trial period, it appeared that the Ministry of Economy, ever anxious to save foreign exchange when U.S. aid was available, was in one way or another coercing importers into using CIP. Under these circumstances there was no way accurately to measure importer preference. Dual licensing was extended into other areas, but by then the reason was the shrinking availability of CIP funding rather than any consideration of economic cost.

#### (4) Open General Licensing

The intent of Open General Licensing (OGL), adopted for a designated list of goods in June and extended eventually to virtually all GVN-financed goods by November 15, was to eliminate the licensing requirement on GVN-financed goods. The move accorded with the general desire of GVN economic leaders to remove economic controls where feasible, and with the piaster at a realistic level, it was thought a good idea to let the market - rather than lower echelon officials at the Ministry of Economy - determine which goods should enter. The evolution of OGL is interesting mainly as a case lesson of what could happen to a system in Viet Nam when the in-

terests of those administering it - here again, those same lower level echelon MOE officials - did not coincide with those of its designers.

Under OGL an importer would purchase an Open General License (since he was buying in advance, this made it, in effect, an advance deposit) entitling him to open a letter of credit for any goods on the OGL list - later, not on the prohibited list - anytime up to one year from the date of his purchase. The system would be subject to spot post-checks only, and importers found utilizing OGL to bring in a banned item would be penalized.

Soon after the system was launched concern was expressed that the post-audit system would not be sufficient protection against unauthorized imports. Moreover, it was argued that some importers would shy away from OGL fearing they later might be accused of, and penalized for, an illegal import. The solution was a questionnaire which an importer could fill in at his option and submit to the Ministry of Economy (MOE). The questionnaire would identify the product the importer intended to bring in: its commodity code, price, supplier country, etc. On approval from the MOE, the importer could proceed in the assurance that his importation would not be questioned later.

There is no question that OGL worked as intended for a while, and that it did have a salutary effect in freeing up the import trade. But gradually, imperceptibly to the American observers, the "questionnaire" evolved into an import license. The importer came to know that a "questionnaire" was expected of him. No decree had been necessary to let him know it.

(5) Subsidies and Protection

In line with its liberal <sup>e/</sup> economic philosophy, the GVN economic team was determined to eliminate import subsidies - that is, have all imported goods priced at least equal to their world market value - and keep domestic industry protection to a minimum. In the former regard, it proved quite ruthless, allowing such necessities as wheat, flour and sugar (a necessity in Viet Nam, at least) to rise dramatically via the exchange rate or import taxes. The wonder is that the rise in the overall price level was so moderate in 1971.

On protection, it proved more equivocal. It appeared rather soon after the November 15 reforms that 25 percent was not much of a basic protection rate for a country in Viet Nam's primitive state of industrial development, and in the case of the textile industry even 50 percent was not adequate to prevent serious damage from competing Japanese and French fabrics. The onset of the 1972 recession made the 25 percent protection limit increasingly untenable and it was breached in a number of areas.

G. Economic Activity, 1971

1971 was a good year for the economy and one in which substantial change was taking place.

(1) Agriculture .

Agricultural output rose by about 13 percent overall. Rice production was up 11 percent to 6,100,000 M/T of paddy, a level 42 percent above the 1966 low point. The 1971 increase was due chiefly to the further increases in the hectareage sown to IR-8 varieties. About 200,000

---

<sup>a/</sup> The term "liberal" is intended here in the classic sense of the term; i.e. a minimum of economic controls.

164

hectares were converted to IR-8 in 1971 for a total to date of 675,000. By 1971 IR-8 varieties accounted for an estimated 2,650,000 M/T of output, or 42 percent of the total crop.

Rice imports in 1971 were down to 160,000 tons of milled rice and there was a stock drawdown of 90,000 tons. Adding in the 75,000 tons required annually merely to accommodate population growth, there would need to be about a 325,000 M/T increase in production (550,000 tons of paddy equivalent) to reach theoretical self-sufficiency in 1972. In practice, more than that would probably be needed, since farmers would withhold stocks from the market when they perceived the tightness of the situation. In any event, it was not to happen.

## (2) Industry

Although results were uneven, the industrial sector made some progress during 1971. The NIS index of industrial production rose only 2½ percent, but this index was biased by the heavy weighting (45 percent of the total index) given the beverage industry. Beer and soft drink production declined slightly in 1971, a result of the U.S. force withdrawal. An alternative USAID index<sup>e/</sup>, based on 11 industries, showed a four percent increase in 1971. Industries doing well were textiles, helped partly by completion of the post 1968 reconstruction with modernized equipment, partly by a general decline in smuggling, and cigarettes, which also benefited from reduced smuggling (in this case, via the PX system).

### a. Industrial Development Bank

An important institutional development in 1971 was the transformation of the old Industrial Development Corporation (IDC), formed in 1957, <sup>e/</sup> From hereon, the USAID index, which was started in 1973 but carried back to 1970, will be cited in lieu of the NIS index. The latter, based on 1962 weights, had become unrealistic.

165

into an Industrial Development Bank (IDB). By 1972 the IDB had cast off its traditional responsibilities such as technical feasibility studies, basic economic research, industrial development and promotion, and assistance in project implementation to emerge as an institution charged with the provision of long-term loans and equity financing. Within four years, with the assistance of a U.S. consulting firm, the C.W. Robinson Company, the IDB became recognized as a seasoned development bank with an experienced staff and had attracted loans from international lending institutions.

b. Divestiture

Another noteworthy development in 1971 was the formal start of a divestiture program whereby ownership of GVN-owned companies was to be transferred to private hands. Eleven companies were identified as initial candidates for divestiture, ranging from the tiny Vinh Hao Mineral Water Company to some of Viet Nam's largest, such as SICOVINA (textiles), COGIDO (paper), and the Ha Tien Cement Company. The purpose was to expand the role of the private sector in industry, and to provide an outlet for the Land Reform bonds being issued to former landlords under the Land-to-the-Tiller Program. A U.S. firm, the Thomas Miner Company, was contracted to assist in the technical aspects of the program.

Two small companies, Vinh Hao and the Thuy Tinh Glass Company, were successfully divested before the program began to bog down. The problem was partly one of valuation, the price to be put on the companies, which proved to be exceedingly difficult in the circumstances prevailing in

166-

Viet Nam, partly a general misunderstanding between GVN and USAID officials as to the appropriate role of divestiture in the GVN's overall economic program. The program snagged on the proposed divestiture of the Viet Nam Sugar Company in mid-1973. At that time, the GVN had stopped importing sugar and was trying to promote the growth of cane toward the end of self-sufficiency. USAID was able to persuade the GVN that in the case of sugar the national interest ruled against a sale to private interests. In mid-1974 the divestiture program was shifted to the Ministry of Planning. Shortly thereafter the future of the divestiture program became linked with the establishment of a national securities market, then in the organization stage. It was felt that any further divestitures should await formal establishment of a securities market. The latter had not been effected by the time Saigon fell.

(3) GNP and Goods Availability

On balance, GNP in 1971 rose by four to five percent. This probably did not translate into increased consumption, as overall goods availability appears to have been about the same as in 1970. The increase in domestic production was offset by a decline in imports. Legal imports rose by 4.5 percent, but after allowance for increases in world prices, there was probably no gain in real terms. Meanwhile, the volume of goods entering the country illegally declined by an estimated \$50 to \$100 million. This was attributable both to better control procedures at the ports and to the reduction in the U.S. force level which, quite simply, meant a smaller potential supply.

(4) Manpower and Employment

The labor market began to ease in 1971. This was attributable in

part to a slowdown in the GVN force buildup as the 1,100,000 force target was neared. While replacement requirements continued to run high, only about 50,000 new personnel were added to the armed forces in 1971. The civil service, on the other hand, increased its rolls by around 100,000 as it moved to meet the increased demands brought upon it by the Vietnamization program. The main factor of ease was a 25,000 decline in the number of people directly employed by the U.S. sector. As many as 25,000 more may have withdrawn from "indirect" U.S. sector employment.

A significant development on the employment front in 1971 was the the launching of/ Association For the Development of the Da Nang Area (ADDA). provide  
ADDA was formed to /public works employment in the Da Nang area which had been hard hit by the U.S. force withdrawal. Its activities were to expand steadily, both in area and in scope as the recession deepened in 1973-74 (see Section XIV,T).

In general, it appears that the net of all these factors was an employment increase of somewhat less than the natural addition to the labor force. During 1971, the population rose from an estimated 18.3 million to 18.8 million, and the labor force from 6.9 to 7.1 million.

(5) Money Supply and Inflation, 1971

a. Monetary Gap

The money supply in 1971 increased by 28 percent, but after allowing for a VN\$9.6 billion increase in piaster balances held by the U.S. Disbursing Officer, mostly in December, the Gap - i.e. that portion of the money supply increase actually put into circulation - was only 22 percent. The principal factors for 1970-71 are summarized below:

	<u>Billions of Piasters</u>	
	<u>1970</u>	<u>1971</u>
<u>Expansionary</u>		
GVN Expenditures	187	256
(Military)	(122)	(151)
(Civil)	( 65)	(105)
U.S. Expenditures	53	81
Exports	2	4
Invisibles	10	14
Credit Expansion	<u>15</u>	<u>24</u>
Total	267	379
<u>Contractionary</u>		
Imports	82	114
Revenues	123	179
(Domestic)	( 52)	( 68)
(Import)	( 71)	(111)
Invisibles	11	19
Advance Deposits	14	-13
Savings	11	33
Other	<u>2</u>	<u>12</u>
Total	243	344
<u>Errors and Omissions</u>	-2	1
<u>Gap</u>	22	36
<u>Plus: Change in DCD balances</u>	-	10
<u>Change in Money Supply</u>	22	46
<u>Gap as Percent of Money Supply at</u> <u>    Previous Year-End</u>	16%	22%
<u>Percent Inc. in Consumer Prices (NIS)</u>	32%	15%

The primary expansionary factor in 1971 was GVN budget expenditures, which rose to VN\$256 billion, or 37 percent over the 1970 level. U.S. piaster expenditures also rose, from VN\$53 billion in 1970 to VN\$81 billion in 1971, mainly because of the higher exchange rate available for personal accommodation. On the contractionary side, GVN domestic revenues were up moderately, from VN\$52 billion in 1970 to VN\$68 billion, or about 32 percent. Although this was a gain in real terms, the first such gain in several years, it fell short of the increase in GVN expenditure, so that the fraction covered by domestic revenue fell slightly. Imports remained the main counter to inflationary pressure. Total import absorption rose from VN\$166 billion to VN\$212 billion, or about 28 percent. Most of this increase stemmed from the exchange rate and tax measures taken in late 1970.

The growth in money supply would have been much greater in 1971 had it not been for the absorption of about VN\$27 billion into time and savings deposits. About VN\$17 billion of these new deposits were placed in Treasury Bills during the year, and these, together with some VN\$4 billion in Treasury Bonds sold to the public, helped to hold down the inflationary impact of the GVN's deficit.

b. Prices

The increase in consumer prices amounted to 15 percent from beginning to end of 1971. This was the best one-year performance since the force build-up began in earnest in 1965. The relative price stability in 1971 was remarkable considering the exchange rate measures and the numerous price increases decreed by the government. A USAID study, based on

the period March 1971 to March 1972, showed that of the 23 percent increase in retail prices during that time, slightly over 19 percent could be ascribed to directed price increases. Domestic rice prices, one area affected--and far and away the most important price index item in terms of weight--rose by 50 to 55 percent during 1971. Among other products affected directly by government action were sugar, beer, soft drinks and cigarettes.

(6) Banking and Credit

a. Saigon Banks Role in Deficit Financing

As shown in the Gap results, Section 5(a), bank savings deposits rose in 1971 by VN\$ 33 billion; of this sum VN\$31.2 billion was accounted for by the Saigon banks and VN\$1.5 billion by the Agricultural Development Bank (ADB) and private rural banks. The increase in savings deposits, a direct result of the Interest Rate Reform of September 1970, enabled the banking system, for the first time, to play an important role in helping to finance the government's deficit.

In 1970 the budget deficit had been financed almost entirely by the National Bank; commercial banks had purchased only VN\$1 billion of Treasury bills. In 1971, thanks to the influx of savings deposits, the banks had been able to take VN\$17 billion of Treasury bills and also expand their loans to the private sector by VN\$2<sup>1</sup>/<sub>2</sub> billion. The credit expansion would have been necessary anyway to finance the increase in import absorption resulting from the ongoing devaluation; it would have been accomplished by rediscounting or through a relaxation of loan: deposit ratios. With the increase in savings activity, it was possible to direct almost half of the total credit increase to the government without

such measures.

(6) ADB and Rural Banks

Banking activity in the rural sector of the economy recorded sharp advances in 1971. Total loans outstanding of the 47 branches of the Agricultural Development Bank (ADB) and the 25 private rural banks rose from VN\$6.2 billion at the end of 1970 to VN\$9.3 billion, an increase of 50 percent. Savings and time deposits rose from VN\$347 million in 1970 to VN\$1,526 million in 1971. The major factor in this growth was, again, the impetus given to the banking sector by the September 1970 interest rate reform. Another contributing factor was the ADB's program to promote the opening of a private rural bank in each of the country's 250 districts. The program initially began as a pilot project in 1969. Three banks were opened in 1969 and only one in 1970. During 1971, however, 21 private rural banks were opened, and another 44 would be opened by the end of 1972.

Rural credit in Viet Nam continued to be supplied primarily through relatives and friends and other non-institutional sources, rather than through organized institutions. However, an estimated 13% of rural credit in 1971 was provided by the ADB and private rural banks, compared with 6% in 1967.

(7) Balance of Payments

Following is a breakdown of the principal balance of payments items during 1969-71:

1721

Simplified Balance of Payments, 1969-71  
(U.S. \$ Millions)

	<u>1969</u>	<u>1970</u>	<u>1971</u>
<u>Balance of Trade</u>			
Exports	15	12	12
Imports, c.i.f.	<u>-689</u>	<u>-692</u>	<u>-714</u>
Balance of Trade	-674	-680	-702
<u>U.S. Support</u>			
U.S. Aid	265	302	340
(CIP)	(177)	(181)	(259)
(P.L. 480 Title I)	( 88)	(121)	( 81)
U.S. Piaster Purchases	347	318	403
(Official)	(301)	(278)	(271)
(Personal)	<u>( 46)</u>	<u>( 40)</u>	<u>(132)</u>
Total U.S. Support	612	620	743
<u>Net Invisibles and Others</u>	5	27	-35
<u>Change in GVN Reserves from OPS</u>	-57	-33	6

The trade deficit rose in 1971 to \$702 million on the strength of a 3.2 percent increase in imports (including A.I.D. freight). Far more than offsetting this was an \$85 million increase in U.S. sector piaster purchases, notwithstanding the 40 percent decline in the average force level mentioned earlier. This seemingly extraordinary development had several explanations, to wit:

a. official expenditures remained virtually unchanged in piaster terms; the effect of inflation on piaster costs offset a 15 percent decline in real outlays (which, as mostly fixed costs, tended to decline far less rapidly than the decline in the force level);

b. the exchange rate for official purchases remained unchanged throughout 1971; it was the only rate left untouched by the November 15 devaluation;

c. per capita personal expenditures of the troop and con-

tractor personnel rose dramatically in reaction to the more favorable accommodation rate (See Section X,D (2) above), more than offsetting the effect of the reduction in force level;

d. the U.S. Disbursing Officer purchased \$23 million worth of piasters in excess of his 1971 needs late in the year (H.B.: This is the counterpart of the spurious increase in money supply noted in Section G (5) a above). His future requirements would decrease accordingly.

For the GVN it was the highest level of earnings from U.S. piaster purchases of the U.S. involvement. Considering the sharp drop to come in 1972, they would have done well to bank more of it than the mere \$6 million increase in exchange reserves in 1971.

#### (8) Exports

Exports in 1971 showed no increase over the 1970 level of \$12 million. It might appear from this that the increase in the export rate--from 118:1 to 275:1 in October 1970 and 350:1 in August 1971--had no effect. This is not the case. In the first place, a decline in world rubber prices cost Viet Nam about \$3 million in 1971. Rubber exports by volume rose by 45 percent. In the second place, new investments in the fishing and lumbering industries could be expected to bring initial results in 1972. As an early indication of this, exports were \$5.4 million in the first quarter of 1972 alone.

#### H. U.S. Aid

U.S. assistance deserves separate mention here if only because 1971 was to be the high-water mark for import support. By the term "import support" is meant U.S. aid to finance commer-

cial imports (CIP and P.L. 480) and piaster purchases. After 1971, piaster purchases would decline precipitously. CIP would average close to the 1971 level at least in nominal terms, although declining drastically in real terms.

In mid-1971 the future development of these factors was less than certain. At one point in July, the foreign exchange outlook appeared sufficiently worrisome for USAID to shift POL and cement, together involving imports of \$95 million a year, to the CIP Positive List. Later, in February 1972, the focus of concern had switched to A.I.D. availability and cement was put back under GVN financing.

I. Jan.-Mar. 1972

For analytical convenience, this Section has focussed mainly on economic developments in 1971 and little has been said of the few months preceding the communists' Easter offensive. There are a few points worth making, however, as it was an unusual period in its own right.

During the first quarter of 1972 the economy was feeling the initial effects of the November 15 devaluation. Moreover, the GVN took a number of additional measures in the exchange rate and tax areas (See Section E above), which had the effect of directly increasing prices of petroleum products (POL), fertilizer, and utility rates. These factors help to explain a seven percent increase in retail prices during the period.

There were also signs of reviving speculation in black market rates and in import licensing activity (in Viet Nam, devaluations--formal or de facto--invariably were followed by increased import licensing). Import licensing was especially heavy in January and was notable in fin-

ished textiles and other luxury items. Licensing levels did not seem to be sustainable in terms of market demand and, in fact, a distinct cooling could be seen by March, as these figures show:

	Import Licensing, 1972 (\$ Million)	
	<u>GVN</u>	<u>CIP</u>
January	31.4	43.7
February	25.8	16.0
March	26.1	22.1

Also by March, businesses and banks were reporting a widespread surfeit of inventories. The economy appeared to be heading for a period of slowdown, ascribable not only to the inventory situation, but also to the ongoing withdrawal of the U.S. forces and the concomitant decline in U.S. sector employment. In short, the Republic was enjoying something less than clear sailing even before the roof fell in with the Easter offensive.

#### XI. Misfortune Befalls, 1972

The invasion of the South by Hanoi's forces, launched on March 31, 1972, was but one of several horrendous misfortunes to occur, or originate, in 1972. Besides the Easter offensive itself and a bad rice crop, the effects of which would be pretty much confined to 1972, these were the U.S. force withdrawal and concomitant decline in import support, and the worldwide inflation in commodity prices.

##### A. NVA Offensive

The North Vietnamese offensive, launched March 31, 1972 and continuing into June 1972, had immediate and severely damaging consequences for the economy. Physical destruction was extensive. Two province capitals, dozens of lesser towns and villages, more than 200 bridges, and many miles of highway were devastated. About 40 percent of Viet

Nam's rubber output was stopped by fighting in plantation areas. More than 1.2 million people left their homes and productive occupations and became refugees.

Another serious effect of the offensive was its impact on private sector confidence. Consumers reacted by cutting down on deferrable expenses, businessmen immediately put off investment projects and began attempting to reduce inventories. The combined effect of the above factors was a serious recession. Many small shops and manufacturing enterprises shut down entirely, and larger businesses laid off workers or went on shortened work weeks. The recession reached a low point around June and there was a gradual recovery during the last part of the year. However, the recovery was far from complete by year end, and several industries, including construction, textile manufacturing, and the wholesale trade in durable goods, remained depressed.

B. U.S. Force Withdrawal

The economic effects of the U.S. force withdrawal, largely delayed for the reasons stated in section X, G (7) above, began to be felt in 1972. Some 47,000 persons were discharged from U.S. sector employment in that year and probably as many more indirectly employed also lost their means of support. There was no increase in the level of GVN employment--either civil or military--so this area did not provide the usual employment offset.

In retrospect, economists would agree that they had underestimated the economic impact of the wholesale loss of jobs caused by the U.S. withdrawal. Perhaps, if business conditions had been normal (for Viet Nam), those discharged could have been absorbed with relatively little

effect. As it was, with recession underway for other reasons, the effect was devastating. Those employed in the U.S. sector had been relatively well compensated. The "ripple" effect of their loss of purchasing power was, therefore, especially pronounced. It was particularly noticeable at and around areas with a formerly large U.S. presence, such as Da Nang, Nha Trang and Qui Nhon, but all urban areas were affected.

On the foreign exchange side, U.S. sector piaster purchases fell to \$213 million from the peak level of \$403 million reached in 1971. The decline was more than accounted for by the change in the official U.S. purchase rate, which had remained at 118:1 after the Economic Reform measures of November 15, 1971. On April 1, 1972, in response to mounting pressures from U.S. Congressional sources, the official purchase rate was changed to accord, henceforth, with the Financial Rate--at that time, 410:1. Personal purchases also declined in 1972, although not nearly in proportion to the 71 percent drop in the average force level, as the per capita expenditures of the troops continued to rise strongly.

C. Decline in U.S. Aid

The decline in U.S. piaster purchases was, of course, foreseen from the time of the Midway Conference in 1969. In May 1971, top U.S. economists from Saigon and Washington met in Singapore for a three-day conference to discuss this eventuality along with other aspects of Vietnamization and the Vietnamese economy. The participants could not know of the external calamities that would befall Viet Nam beginning in 1972, but in no area was there to be a greater frustration of expectations than in the area of piaster purchases and U.S. aid.

At Singapore, the forthcoming decline in piaster purchases was viewed as an opportunity, not as a menace. It was assumed that the decline in purchases would be matched by an increase in grant aid, and that Viet Nam would thereby earn a "resource dividend" from the freeing of manpower and materials previously employed, or utilized, by the U.S. sector. The discussion turned on how best to take advantage of this "dividend". There was no consideration that U.S. aid might not rise to offset the decline in piaster purchases, let alone that U.S. assistance, in real terms, would decline drastically. Under the circumstances, the "resource dividend" would become a steadily growing body of the urban unemployed.

The trend in aid from 1972 through 1975 will be covered below. Here it will suffice to note that U.S. import support declined from \$849 million in 1971 to \$591 million in 1972, as follows:

	<u>U.S. Import Support, 1971-72</u> (\$ Millions)	
	<u>1971</u>	<u>1972</u>
CIP (FY)	281	313
PL 480 Title I (FY)	165	63
Direct Dollar Support	-	2
Piaster Purchases (CY)	<u>403</u>	<u>213</u>
Total	849	591

D. Import Prices

Until 1972, the movement in the prices of goods imported by Viet Nam was literally so slight as not to be deemed worthy of notice. That is, import data could be treated in nominal terms without the need to correct for the effect of inflation. Using U.S. export prices as an indication of the movement of these prices, they can be seen to have risen

by only 21.4 percent in the eight years, 1963-71, which translates to an average annual rate of only 2.45 percent. The beginning of a new era was signalled by the Smithsonian Agreement of December 1971. Overnight the Japanese yen, to mention Viet Nam's second largest supplier (after the U.S. itself), appreciated by 16.9% relative to the dollar. By mid-1972 prices of international commodities were rising on a broad front. For 1972 as a whole, Viet Nam's import dollar was worth ten percent less than in 1971: the decline for 1971-74 would amount to 54 percent.<sup>a/</sup> Applying the 1971-72 import price increase to the import support data shown above, the decline in real U.S. import support from 1971 to 1972 was one of 37 percent.

E. Rice

Still another misfortune, this one fortunately not of a continuing nature, was the poor 1972-73 rice crop. After three successive years of excellent harvests, the 1972-73 crop suffered from inadequate rainfall during the early planting season and, at 5.9 million tons, was off three percent from the 1971-72 crop. Imports rose from 140,000 tons in 1971 to 284,000 tons in 1972.

F. Economic Activity

The continued effect of the NVA offensive and the U.S. withdrawal was a general recession, which was at its most severe in the second quarter of 1972. The index of manufacturing production for the year, as a whole, was off four percent from 1971. Reflecting the generally de-

---

<sup>a/</sup> Beginning with 1972, all measurements of import prices are Mission calculations based upon the principal commodities in Viet Nam's import trade.

pressed business climate, import demand fell sharply. Combined GVN and CIP licensing (omitting PL 480 data which are less indicative of business activity) for the period April-December 1972 was 23 percent below the corresponding 1971 period. Construction activity was greatly depressed, especially in urban areas.

In the agricultural sector, with rice production off three percent from 1971 and rubber production sharply reduced by the NVA offensive, overall output declined by an estimated two percent from the 1971 level. On the other hand, the fish catch and timber cuttings registered good gains over 1971.

G. National Income

GVN national account statistics show a nominal decline of 0.2 percent in GNP for 1972, which would in turn translate to a per capita decline of nearly three percent. Considering that legal imports declined by 14 percent in real terms and that there was undoubtedly a further drop in illegal imports (smuggling) as well, the decline in goods availability was undoubtedly greater than this--five percent or more. The burden fell most heavily on the city dwellers and, even more, on GVN employees. After two years, 1970-71, in which the long decline in real GVN wages had been temporarily halted, the slide was underway again. In 1972 wages rose only 14 percent, consumer prices 27 percent.

H. Self-Help Measures

Not all the news in 1972 was bad. Progress was shown despite declining aid in exports, tax reforms and other self-help measures.

(1) Exports

As noted, the effort to raise exports, which began with the partial

devaluation of September 1970 had not shown results, in terms of export earnings, in 1971. In 1972, however, the investments made in 1971 began to pay off. Exports nearly doubled, from \$12 million to \$23 million. Leading the way were rubber with \$7.2 million; fish products (mostly frozen shrimp)--\$5.5 million; and lumber--\$3.0 million. The GVN pursued a policy of vigorous export promotion (by the standards of previous years, if not necessarily by that of other developing countries). In May the export rate was set at 500:1, providing an 80 piaster premium over the official rate. The export rate was raised to 550:1 in July where it remained for the rest of the year. The export premium ranged from 120 piasters (28 percent) in July to 85 piasters (18 percent) at the year-end. From July on an additional 25 piaster subsidy was provided for the export of products new to Viet Nam.

(2) Tax Reform

Domestic tax revenues in 1972 registered the first meaningful year-to-year increase of the entire period of U.S. involvement, a 45 percent gain on the 1971 results. Since prices rose by only 27 percent, this was also an improvement in real terms. The achievement, which was the more remarkable considering the economic climate in which it occurred, was attributable partly to a broad revamping of the tax structure and partly to a wholesale shake-up of Tax Directorate personnel.

Under special powers legislation granted him in the wake of the NVA offensive, President Thieu issued a number of tax measures in the six months ended December 27, 1972. Taken as a package, these measures constituted a basic reform of the entire GVN domestic tax system.

The more significant of the new tax measures were:

--Tariff Schedule - The law made de jure the tariff schedule adopted in November 1971, as part of the major reform of the exchange system undertaken at that time. (See Section X,E above).

--Property Taxes - The new law replaced a tax that was levied, for the most part, in absolute amounts at rates that had become negligible. The new rates were to be based on continued assessments on an ad valorem basis, with revenues accruing to local governments.

--Motor Vehicle Tax - Rates were raised on all classes of vehicles.

--Income Tax Code - The tax incorporated four earlier taxes on income. The corporation tax was fixed at a flat 45 percent, the income tax at rates graduating from 10 to 70 percent.

--Value Added Tax - The VAT, decreed July 1973, was to become the most important single revenue producer. (See Section XII, R(2) below for the evolution of VAT in Viet Nam.)

--Special Consumption Tax (SCT) - This tax, which would be the second most important revenue producer, consolidated existing excise taxes, perequation taxes, and other miscellaneous taxes into a single ad valorem tax ranging from 10 to 128 percent, levied on certain goods, notably tobacco, beer, soft drinks and POL.

### (3) Other Self-Help Measures

Other reforms were largely institutional. A new investment law, promulgated in June 1972, was put into operation. An Investment Committee at cabinet level and an Investment Service Center were established. Though few foreign investors were coming to Viet Nam in 1972, the GVN

was ready to offer benefits such as tax concessions substantially equal to those offered by other countries in the region. A National Economic Development Fund (NEDF) was also established in March 1972 as a rediscount facility with preferential interest rates, offering financing to approved investments, whether of domestic or foreign capital. By the end of 1972 NEDF had committed 7.9 billion piasters from its original funding of VN \$10.0 billion.

I. Balance of Payments

The balance of payments results were dominated by two factors: the \$190 million drop in piaster purchases noted above, partly offset by a \$98 million decline in GVN-financed imports. There was an \$11 million overall deficit. The items involving foreign exchange in 1971 and 1972 are summarized below:

Balance of Payments - Foreign Exchange Items Only  
(U.S. \$ Millions)

	<u>1971</u>	<u>1972</u>
<u>Receipts</u>		
Exports	12	23
Piaster Purchases	403	213
Direct Dollar Support <sup>a/</sup>	-	16
Invisibles	70	81
POL Reimbursements Less Advance Payments <sup>b/</sup>	<u>-</u>	<u>8</u>
Total	485	341
<u>Payments</u>		
GVN Imports	374	276
Invisibles	87	76
Advance Payments for POL Less Reimbursements <sup>b/</sup>	<u>18</u>	<u>-</u>
Total	479	352
<u>Change in Reserves from Operations</u>	6	-11

<sup>a/</sup> Direct dollar support under the A.I.D. authorization for humanitarian (primarily refugee relief) purposes. Note that the direct dollar support figures shown in balance of payment summaries will not agree with the corresponding data on Table I, as the latter are on an obligation basis.

<sup>b/</sup> Under the prevailing method of financing GVN paid in advance for POL shipments subject to later reimbursement from AID/W.

J. Monetary Gap and Inflation

(1) Monetary Gap

The monetary increase as measured by the Gap was a moderate 15 percent<sup>c/</sup> in 1972. GVN expenditures rose by VN\$ 110 billion, or 43 percent. Military and other war-related expenditures, such as veterans' benefits and refugee costs, were the principal factors. The increase in domestic tax revenues, impressive as it was, could not keep up with the increase in expenditures in absolute terms; however, domestic revenues, as a percentage of expenditures, rose from 26.6 percent in 1971 to 27.3 percent in 1972. Import taxes were sharply down owing to the November 1971 reforms by which the bulk of import revenues were shifted from import taxes to the exchange rate. Import absorption as a whole-- imports plus import taxes-- rose by VN\$ 55 billion, or 24 percent. Most impressive, savings and time deposits at the commercial banks continued to rise sharply. The increase in 1972 was one of VN\$ 66 billion, or 68 percent of the increase in money supply and savings combined.

The Gap results for 1971-1972 are shown below:

<sup>c/</sup> The money supply actually rose by only nine percent, but the formal accounting failed to take account of VN\$ 9.6 billion of piaster balances held by the U.S. Disbursing Officer (and shown in the formal money supply) at the end of 1971 and put into circulation in 1972.

MONETARY GAP 1971-72  
(VN\$ Billions)

	<u>1971</u>	<u>1972</u>
<u>Expansionary</u>		
GVN Expenditures	256	366
U.S. Expenditures	81	96
Exports	4	11
Invisibles	14	26
Credit Expansion	<u>24</u>	<u>31</u>
Total	379	530
<u>Contractionary</u>		
Imports	114	233
Revenues	179	147
(Domestic)	( 68)	(100)
(Import)	(111)	( 47)
Invisibles	19	24
Advance Deposits	-13	1
Savings	27	66
Treasury Bond Holdings of Individuals	4	6
Other	<u>14</u>	<u>23</u>
Total	344	500
<u>Errors and Omissions</u>	1	1
<u>Gap</u>	36	31
<u>Plus: Change in DOD Balances</u>	10	-12
<u>Change in Money Supply</u>	46	19
<u>Gap as % Money Supply at Previous Year End</u>	22%	15%
<u>% Inc. in Consumer Prices (CPI)</u>	15%	27%

(2) Prices

Consumer prices rose 27 percent in 1972, markedly more than the 15 percent rise in the Gap. Principal factors in the increase were rice price increases on the order of 35 to 40 percent, attributable to the tight supply situation and to distribution problems related to the increased hostilities, and the effect of price increases decreed by the GVN early in the year (See Section X,E above). Also, higher prices of imported goods were beginning to have an impact. Besides the nine percent increase in the dollar cost of imports, the exchange rates applicable to both GVN and CIP-financed goods were devalued by 16 percent in 1972 for a combined piaster cost increase to the importer of 26 percent (1.09 x 1.16). The increased cost of imported goods would become a major issue in 1973.

XII Recession, Aid Decline, and The Struggle For Self-Sufficiency, 1973-74

As 1973 began there were grounds for cautious optimism. The North Vietnamese offensive had been driven back and resettlement of the latest wave of refugees was proceeding smoothly. The worst of the 1972 recession appeared to be over; in fact, the available indicators showed signs of a recovery beginning in the fourth quarter of 1972. The economy, at any rate, appeared to be making an orderly, if frequently painful, adjustment in the direction of self-sufficiency. The final effects of the U.S. withdrawal--both on employment and on foreign exchange earnings--had yet to be reckoned with, but exchange reserves were still at a high level and there was hope of an increased aid appropriation. There was increasing talk of economic development, and a number of promising insti-

tutional developments--the activities of the new Planning Ministry, the formation of NEDF--appeared to lend substance to the talk. It was hoped that foreign investors would finally respond to the country's undoubted economic potential.

As matters were to turn out, the country's troubles had barely begun. Looking back, at the end of 1973, there were promising developments to point to in rice production, exports and rising tax revenues, to name a few. By the end of 1974, however, virtually all of the best efforts of the policy-makers were on the verge of being undone by the combined effects of world-wide inflation and declining real aid levels.

A. U.S. Withdrawal Completed

The last of the U.S. troops departed Viet Nam on March 28, 1973, shortly after the signing of the Paris Agreements. U.S. piaster purchases fell from \$213 million in 1972 to \$96 million in 1973 and \$97 million in 1974. That there remained any piaster purchases at all was due, first, to continuing purchases by civilian agencies and the remaining civilians as individuals and, second, to DOD programs that remained in force after the withdrawal was completed. The programs in question were: (1) the AID/DOD Realignment Program, whereby the DOD funded on a reimbursement basis certain programs mostly in the area of highway maintenance carried out through the Foreign Aid Chapter (formerly the American A.I.D. Chapter) of the GVN budget; and (2) the Local Procurement Program, whereby the DOD purchased certain locally produced goods for transfer to the Vietnamese Armed Forces under the Military Assistance Support Funding (MASF) program. The Local Procurement Program, begun in 1971, never

189

lived up to the original expectations of earnings of at least \$100 million. It was dogged from the start by problems relating to quality control, failure of producers to meet delivery deadlines, unrealistic bidding and, above all, a failure of producers to allow for the effects of inflation. Nevertheless, the program was a significant foreign exchange earner and provided a prop to the economy when it was needed most.

The amounts transferred under these two programs in 1973 were: AID/DOD Realignment, \$17.4 million; Local Procurement, \$28.7 million. The corresponding data for 1974 are not available.

Another 40,000 persons were discharged from U.S. sector employment in 1973, bringing the number remaining employed at year-end to about 15,000. Employment was at a peak of 160,000 in June 1969. The impact of the discharges was more severe in 1973 than in 1972, simply because of the cumulative effect of loss of purchasing power. It is believed to have been the principal factor in the deepening recession.

B. Increase in World Prices

The increase in world prices that began in 1972 accelerated in 1973 and through the first quarter of 1974. World-wide inflation hurt all developing countries during this period, but its effects were especially severe in Viet Nam's case. This was partly because Viet Nam happened to be heavily dependent on a number of commodities most severely affected by the inflation, partly because of the lopsided nature of Viet Nam's trade. With imports 20 times the value of exports, Viet Nam could not regain on the export side what it gave up on the import side. Moreover, the overwhelming importance of imports in the Vietnamese economy --Imports were

190

roughly a third of GNP--meant that the shock of import price increases was felt to an especially great degree in all sectors.

A Mission study early in 1974 showed that the prices of six commodities--rice, petroleum (POL) products, fertilizer, sugar, cement and steel--that accounted for 34 percent of Viet Nam's import trade, rose an average of 80 percent from mid-1972 to the end of 1973. The average of all import prices in 1973 was 35 percent higher than the average of all import prices in 1972; and the increase from 1973 to 1974, similarly accounted, was an incredible 53 percent. Thus, import prices more than doubled ( $1.35 \times 1.53 = 2.06$ ) during 1972-74.

C. U.S. Aid

With President Thieu scheduled to travel to San Clemente for a meeting with President Nixon in March 1973, Vietnamese and U.S. Policy-makers debated strategy for an A.I.D. request that would best balance the country's needs and the reality of a doubting Congress. The planners could identify three distinct categories of need: a minimum level of aid needed to preserve the status quo; an additional amount required for reconstruction and resettlement of refugees in the wake of Hanoi's 1972 offensive; and a further amount to provide a start on economic development. The debate was on the priorities to be accorded the three areas and the extent to which either or both of the last two should be sacrificed in the name of political realism.

The Vietnamese decided to go for all of it. As preparation for the President's San Clemente trip, they produced a well-considered, if optimistic, study of the economy during the period 1973-80. The study indicated a need for foreign assistance--defined not to include U.S. piaster

-191-

purchases--of \$649 million in 1973, \$783 million in 1974 and \$717 million in 1975, tapering off, thereafter, to \$95 million in 1980. All amounts, it should be noted, were stated in terms of 1973 dollars; thus, as events were to show, the \$783 million requirement for 1974 would have had to be \$1.2 billion if the purchasing power of the aid dollars were to be maintained. The Vietnamese paper expressed the hope that third country and institutional aid would be available in rising quantities to help reach these amounts, but as no balance of payments support had yet been received from other than U.S. sources, it was clear that the U.S. would have to foot most of the bill--certainly in the early stages.

While President Nixon gave a broad endorsement to Viet Nam's request, the Congress was less impressed. The FY 1973 A.I.D. appropriation for Viet Nam, after apportionment of Indochina funding among the three Indochina states, was \$313 million. The amount available for CIP funding, after deduction of \$56 million for the Project Program and \$31 million for Refugee Relief, was \$226 million. It was the lowest CIP allotment since 1965, even in nominal terms.

The A.I.D. appropriation was increased in FY 1974 to \$383 million, including a \$50 million Development Loan and a \$49 million Supplemental Appropriation passed by Congress in June 1974, and USAID was able to fund an additional \$34 million for the CIP Program by cutting the Project Program from \$56 million to \$22 million. Nevertheless, given the aforementioned 53 percent rise in import prices, the real result was another sharp reduction in the aid level. Import support, defined as CIP, PL 480 Title I, Direct Dollar Support (refugee relief), and Piaster Purchases

declined in all by 62 percent from 1971 to 1974;

U.S. IMPORT SUPPORT, 1971-74  
(\$ Millions)

	(1) CIP	(2) PL 480 Title I	(3) Refugee Funding	(4) Piaster Purchases	(5) Total Import Support	(5) Import Prices (1971= 100)	Real Import Support (\$ 1972)
1971	281	165	---	403	849	100	849
1972	313	63	2	213	591	110.7	534
1973	226	179	31	96	532	149.5	356
1974	335	269	26	97	727	228.8	318

Note: CIP, FFP and Refugee Funding on fiscal year basis; piaster purchases on calendar year basis.

D. Other Donor Aid

Third country and international institutions were increasing their aid, but the balance of payments effect was minimal. In 1973 all Other Donor assistance--\$109 million worth--was project aid. In 1974, Other Donor assistance, in commitment terms, rose to \$183 million. Of this amount some \$60 million was balance of payments support from France, Japan and Taiwan. The amount of Other Donor balance of payments support actually utilized in 1974 was \$26 million.

E. Balance of Payments

Despite the reduction in U.S. import support in 1973 and 1974, the nominal value of imports increased in both years: \$678 million in 1972 to \$717 million in 1973 and \$887 million in 1974. There follows a simplified balance of payments summary for 1972-74:

Simplified Balance of Payments, 1972-74  
(U.S. \$ Millions)

	<u>1972</u>	<u>1973</u>	<u>1974</u>
<u>Receipts</u>			
Exports	23	60	75
Piaster Purchases	213	96	97
U.S. AID	418	438	625
(CIP & PL 480 Title I)	(402)	(406)	(622)
(Direct Dollar Support)	( 16)	( 32)	( 3)
Invisibles	81	139	226
Other Donor Aid	---	---	26
• POL Reimbursements Less Advance Payments	8	( -8)	(-39)
<b>Total</b>	<b>743</b>	<b>725</b>	<b>1010</b>
<u>Payments</u>			
Imports	678	717	887
(GVN)	(249)	(281)	(196)
(AID Freight)	( 27)	( 30)	( 43)
(CIP)	(284)	(253)	(419)
(PL 480 Title I)	(118)	(153)	(203)
(Other Donor)	(---)	(---)	( 26)
Invisibles	76	82	86
<b>Total</b>	<b>754</b>	<b>799</b>	<b>973</b>
Change in Reserves From Operations	-11	-74	37
Allocation of SDR's	7	3	---
Errors & Omissions	1	-4	5
Change in Reserves (NEVR)	-3	-75	42
(Commercial Banks)	( -6)	( 5)	( -5)
Reserves, End-Year	269	194	232
1. Official <u>a/</u>	254	174	217
2. Commercial Banks	15	20	15

Note: a/ Includes gold, foreign exchange, and SDR's

194

(1) 1973

Piaster purchases declined by \$117 million in 1973. Offsetting this were \$16 million in Direct Dollar Support for Humanitarian Assistance, the initial funding under the so-called Kennedy Amendment; a \$37 million increase in exports, to \$60 million; and a \$59 million increase in invisible receipts, to \$139 million. However, payments for GVN imports rose by \$32 million and the National Bank drew down its reserves by \$80 million.

The phenomenon of sharply rising invisible receipts was attributable in part to the sale of concession rights to foreign oil companies in August (\$17 million) and to a heavy inflow of short-term capital. The nature of this inflow, which was to continue in 1974, was never certain, but was attributed mainly to tight money conditions and the resulting shortage of domestic credit. Sales of dollars by the Viet Cong may also have been a factor. Of the 1973 total, \$17 million consisted of currency notes turned into the banks--no questions asked. Whether Viet Cong sales or the sales of hard-pressed local businessmen, the one certainty is that these currency conversions would not have taken place had there been a black market currency premium of any significance. <sup>a/</sup> Thus, the tight money policy was, at least, a necessary condition for the conversions.

(2) 1974

Almost alone of all non-OPEC countries, Viet Nam experienced an increase in its exchange reserves during 1974. Apart from the \$67 million

---

<sup>a/</sup> The black market premium on the official rate was in a range of 13 to 17 percent during January - February and again during October - November. For the remainder of the year it was much lower, usually below five percent.

195

of additional oil imports in 1974, reimbursements from AID/Washington lagged behind GVN advance payments for POL by \$39 million, so that the net additional cost of POL to Viet Nam in 1974 was \$106 million. This figure was more than offset by an \$87 million increase in invisible receipts and an \$85 million reduction in GVN imports. The \$226 million of invisible earnings in 1974 included \$30 million from the sale of oil concessions and \$54 million of currency conversions at the banks. Owing initially to the GVN's own restrictions, and later to reduced demand as a result of the recession, GVN-financed imports declined from \$281 million in 1973 to \$196 million in 1974. National Bank reserves rose by \$43 million to \$217 million (gold, foreign exchange, and SDR's) at the year-end.

F. Imports, Nominal and Real

As can be seen in Section E above, imports rose in both 1973 and 1974. The increase in 1974 was to a record \$887 million, a gain of \$160 million, or 24 percent, over 1973. The increase in PL 480 imports was entirely due to increased imports of rice at higher prices. CIP imports fell in 1973 owing to the widespread supply shortages of those years, then rebounded strongly as the shortages eased and delayed shipments took place in 1974. As was the case with import support, the apparent rise in overall imports is illusory. With the data adjusted to allow for higher import prices, it can be seen that real imports declined by 22 percent in 1973 and another 19 percent in 1974. At the 1974 level imports in real terms were barely half of the 1971 level. They were at their lowest level since 1965 and, in per capita terms, at their lowest level since 1964; i.e. the last year before large-scale U.S. involvement.

196.

(U.S. \$ Millions)

	<u>Import Payments</u>	<u>Import Prices (1971 = 100)</u>	<u>Real Imports \$ 1971</u>	<u>1971 = 100</u>
1971	714	100.0	714	100
1972	678	110.7	612	86
1973	717	149.5	480	67
1974	887	228.8	388	54

G. Efforts to Conserve Foreign Exchange

Given the unavoidable reduction in imports, the GVN undertook drastic efforts to eliminate the fat from the import program. In some cases, as in the effort to reduce consumption of POL, they did not stop at the fat.

(1) Non-Essential Imports

Reduction of non-essential, or luxury, imports was not, as it might seem, a simple matter. Direct import controls were anathema to the liberal-minded economists (and even more so, their American advisors) who engineered the 1970-71 reforms. To be sure, the "open General Licensing" system begun in 1970 had not functioned for very long as a truly open system anyway (See Section X,F(4) above). Nevertheless, nearly everyone opposed a return to formal licensing fearing, for one thing, that a ban on luxury imports would only result in their being smuggled in with an attendant rise in the black market rate. Non-essential imports would have to be restricted through indirect methods that, presumably, would do a minimum of violence to the open economy philosophy. Accordingly, from May 1972 to mid-1974 the GVN imposed a succession of indirect measures beginning with high advance deposit requirements, then increased

perequation taxes, and--in February 1974--a ban on the use of bank credit to finance the importation of any goods on the GVN's "C" and "D" lists (i.e. about 80 percent of all imports that could be considered non-essential).

The results were impressive. Using USAID's definition<sup>a/</sup> of the term, letter of credit openings for non-essential imports declined from an annual rate of \$74 million in the second half of 1972 to \$56 million in January - June 1973, \$38 million in July - December 1973, and \$18 million in January - June 1974. Stated in percentage terms, non-essential imports declined from 39 percent of total GVN import demand (total imports adjusted to exclude sugar and cement) in July - December 1972 to ten percent in January - June 1974. On July 1, 1974, foreign exchange considerations having by then become compelling, the GVN dropped Open General Licensing altogether, in the process banning all goods on the "C" and "D" lists. This action left a number of items free to come in, so on August 22, 1974, ten additional categories of goods were added to the banned list. With virtually all non-essential goods by then banned, the GVN could be said to have saved some \$70 million over the amount expended for these items in 1972.

(2) Other Import Reductions: Sugar and POL

Apart from items clearly identifiable as non-essential, cutbacks were made in other areas of a borderline nature. Sugar imports, which cost the GVN \$60 million in 1973, were stopped altogether in 1974.

---

<sup>a/</sup> USAID's definition of non-essential imports was all goods to which advance deposit requirements were applied on 2/22/73 and 3/3/73. The list included virtually all imports that could meet a definition of non-essential.

198

Apart from being consumed in great quantities as a sweet, sugar was a crucial raw material in the beer and soft drink industries. Fortunately, the government came into 1974 with a strong stock position. They were determined to stretch those stocks and avoid imports by drastically reducing consumption. This was done by allowing the domestic price of sugar to rise in line with the skyrocketing world price. Beer and soft drink prices kept pace. As a result, by 1974 the domestic sugar industry was enjoying a strong come back. It was considered possible that by 1976, when carry-over stocks would be depleted, Viet Nam would be self-sufficient--at the reduced rate of consumption--in sugar.

The GVN's reaction to the increase in POL prices decreed by the OPEC countries merits special attention, since perhaps no country in the world made more heroic efforts to reduce POL consumption in this period than Viet Nam.

Rising POL prices raised Viet Nam's import bill for POL from \$60 million in 1972 to \$82 million in 1973, for a volume of imports less than one percent greater. World prices were then raised an average 150 percent by the OPEC measures of November and December 1974. Faced with the prospect of paying \$200 million in 1974 for the same amount of POL costing \$82 million in 1973, the GVN set as its goal a 25 percent reduction in consumption. Domestic POL prices, which had already been raised by 36 to 47 percent in November 1973, were raised another 66 to 140 percent on January 16, 1974. At that point gasoline was priced at the equivalent of \$1.62 per gallon, one of the highest levels in the world. Kerosene, at 140 piasters/liter, was priced out of reach of lower income

families, spurring a mass conversion to wood and charcoal for cooking fuel. Diesel fuel, at 125 piasters/liter, proved so expensive as to idle a large portion of the country's motorized fishing fleet, and the price had to be rolled back to 95 piasters/liter in March. The high POL prices, combined with austerity measures on its use, mostly in the public sector, accomplished the GVN's immediate objective. Consumption in 1974 fell by 25 percent, divided roughly as follows: kerosene, 63 percent; gasoline, 51 percent; diesel, 15 percent; heavy fuel oil, 10 percent.

As a footnote to the GVN's actions in the POL area, it may be noted that the extremely high price of diesel fuel was a very controversial issue at the time. Even at the reduced price of 95 piasters a liter, diesel fuel was priced at a level far above that prevailing in neighboring countries, and there is no question that it affected the competitive position of Vietnamese fishermen. Eventually, all 11 of Viet Nam's motorized shrimp trawlers were idled, mainly for this reason. There was little question that the export earnings foregone more than offset the \$3 million saved in reduced diesel imports. Moreover, the higher diesel cost, where it did not result in actual production losses, did result in higher operating costs, and ultimately consumer prices, throughout the agricultural sector as well as in fishing. As a tax--the only basis on which it could be defended--the high cost of diesel fuel was a highly regressive one, since it fell most heavily on the price of fish.

By mid-1974 GVN officials had come to recognize the overall harmful effect of the high price of diesel fuel but, by that time, were unable to do anything about it. The reasons were partly technical, and will not

be gone into here, partly matters of face and relations with the legislature. The issue pointed up a growing paralysis within the GVN economic leadership which was never to be resolved.

H. Resource Transfers

By cutting their consumption of less essential goods, the GVN was able to mitigate to some extent the effect of the forced reduction in overall imports. However, the meaningful portion of that reduction was still very considerable. There was nothing for it but to shift from import-dependence to self-sufficiency. Necessary to this process was a shift in relative prices to encourage consumption of domestic, as opposed to imported, goods. To this end the GVN continued the "trotting peg" exchange rate policy begun in 1971 (see Section XII,U) for discussion of exchange rate policy), in addition to the advance deposits and increased import taxes applied to non-essential imports. The necessary resource transfers did, in fact, take place in a large number of areas. Thus, wood came to replace kerosene as the principal fuel in cooking, rice straw replaced imported pulp in the manufacture of paper, the sugar industry revived, etc. Mistakes were made as Vietnamese businessmen, once again, followed their age-old practice of plunging en masse into an area in which someone ahead of them had made a killing (e.g. the fishmeal industry, which came from nowhere to nine plants, of which only one was operating by the end of 1974), but alert businessmen, especially those attuned to exporting, could make money. Observers seeing these changes were wont to conclude that it was highly commendatory and just what should have been happening all along.. They were partly right. What they

-201

were liable to overlook though, was the great number of factories closing down for lack of imported materials, or for lack of markets as a result of the general recessionary conditions. The unemployment spawned by shut downs far exceeded the new employment created by the embryo export firms.

In short, the process of change that took place in 1973-74 was necessary and even healthy. The difficulty lay simply in the absence of conditions necessary for a resource transfer of the required magnitude in so brief a period of time. Even simple manufacturing processes based on domestic resources required capital, and there was not much of it coming forward. Moreover, many potentially profitable investments failed to go forward because of poor security conditions; this applied especially to agribusiness ventures in 1974. Thus, resources idled by the reduction in imports and by the low level of investor confidence tended increasingly to remain idle.

#### I. Manufacturing Activity

Industrial activity declined in general owing to shortages of raw materials, reduced demand, high operating costs and, especially in 1974, the government's highly restrictive credit policy. USAID's manufacturing production index declined by 8 percent in 1973 and by 23 percent in 1974. The decline was uninterrupted in 1974, the index for the fourth quarter of 1974 standing at 60 (fourth quarter, 1971=100). In 1973, certain firms producing for the Local Procurement Program or for export, such as glass and plywood producers, continued to do well. By 1974, with recession spreading abroad, these firms had begun to founder. Firms doing worst in 1974 were those catering to less essential needs, such as beer

202

and soft drinks. The textile industry was generally depressed notwithstanding the ban on fabric imports in mid-1974.

J. Agriculture, Forestry & Fishing

(1) Rice

Rice production in 1973 rebounded strongly from the disappointing 1972 crop-year. Production rose 11 percent, to a record 6.6 million tons. The 1974-75 crop was estimated to have risen a further 7.5 percent, to 7.1 million tons. Fertilizer usage by farmers declined by an estimated 30%, but this factor was more than offset by a ten percent increase in the area of rice under cultivation. (Agricultural technicians explained that the major part of the impact from a decline in fertilizer usage is not seen until the year following that decline).

Owing to a low stock position at the outset of 1973--rice stocks were only 57,000 tons--and the propensity of farmers to hold onto their stocks as inflation gained momentum during that year, the excellent 1973 crop did not lead to a reduction in rice imports. On the contrary, rice imports rose from 285,000 tons in 1972 to 305,000 tons in 1973. Imports in 1974 were 300,500 tons, but this was sufficient, even after lending 45,000 tons to Cambodia, to build rice stocks to 205,000 tons as of December 31, 1974. Self-sufficiency, at long last, was a distinct possibility (perhaps a necessity since it was not certain that PL 480 rice would be available in 1975).

One event worth noting in 1973 was the approximate doubling of retail prices, reflecting the upsurge in the world price then underway.

In August, under the threat of short supplies and rising prices, the

system in effect for some years, in which the GVN purchased some rice for distribution chiefly to its employees but left the market generally free, was sharply modified. The GVN took over nearly all rice purchasing and distribution at the wholesale level and attempted to enforce price controls, along with fixed quotas for province delivery to Saigon and a blockade of shipments to communist controlled areas. In December, these measures were largely rescinded.

a. The Rice-Fertilizer Price Issue

A major policy issue in 1974 was the relative prices of rice and fertilizer and the extent to which either, or both, should be subsidized. World prices of both rice and fertilizer rose spectacularly during 1973 and 1974. The retail price of rice was allowed to reflect most of the world price increase, but not all of it. Retail rice prices rose 143 percent (no. 1, 25 percent broken) from the fourth quarter of 1972 through the fourth quarter of 1974 which just matched the rise in consumer prices generally. However, by January 1975, the retail price of Soc Hau, the most common Vietnamese brand, was 23 percent below the Thai price at the prevailing exchange rates, and the GVN did not think it politically feasible to close the gap given the prevailing recessionary conditions. World fertilizer prices, meanwhile, had more than tripled, and domestic fertilizer prices had been allowed to follow them up, rising 285 percent in the same 1972-74 period. The declining rice:fertilizer price ratio had already led to reduced usage in 1974 and threatened the vital drive for self-sufficiency.

The considerations were: (a) raise the rice price to gain the production incentive, meanwhile risking the political reaction, (b) sub-

204

subsidize fertilizer to get the same (presumably) production incentive, but incur a budgetary cost; (c) leave things as they were; (d) try a combination of (a) and (b). Complicating the matter was the fact that the world prices of both commodities were fluctuating widely, making calculations of future subsidy costs virtually impossible.

It was decided in July to subsidize fertilizer at a price deemed necessary to encourage farmers to use it (i.e. at about two thirds of the world price). Rice prices would continue to be raised gradually toward the world level. The fertilizer subsidy, implemented in September 1974, was expected to cost the GVN V\$20 billion a year. It appeared to be working well early in 1975, but a number of economists continued strongly to favor abandonment of the subsidy and higher rice prices, especially so as the budgetary outlook worsened.

(2) Other Crops

Other crops posting good production increases in 1973-74 included sugar, corn, and peanuts. Expansion of sugar output, under the impetus of soaring world and domestic sugar prices, was especially impressive. Total hectareage is estimated to have risen from 13,000 in 1973 to 20,000 in 1974, and artisan mills sprang up by the hundreds. The country reached self-sufficiency in corn, with production rising by an estimated ten percent in 1974. Reliable data were not available on peanut production, but a processing industry had begun to develop and the need for oil imports was declining.

(3) Forestry

The forestry industry did well in 1973 on the strength of export demand, mostly for pine logs, but ran into a wide array of difficulties

in 1974. The world market for lumber and wood products turned soft, many areas were closed to lumbering for security reasons, fuel costs rose sharply and the industry was plagued by bureaucratic restrictions of one sort or another. Exports of logs and lumber fell from \$12.2 million in 1973 to \$9.8 million in 1974, and exports during July - December 1974 were only \$2.3 million.

(4) Fishing

The fish catch reportedly rose by ten percent in 1973, but declined somewhat in 1974 under the impact of high diesel fuel costs (see Section G (2) above) and, in some areas, security restrictions. A large portion of the country's motorized fleet was idle during the year. Declining world prices for shrimp produced a levelling off in export earnings after the first quarter of 1974. For all of 1974, however, exports of fish products reached \$29.4 million, up from \$13.9 million in 1973.

K. Land Reform Program

A development of great significance to the agricultural economy during the 1970's was the Land-to-the-Tiller Program. Begun in March 1970, its formal completion was announced in March 1973. The LTT Program, which is covered in detail in a separate sector paper, resulted in the transfer of some 1.1 million hectares of land, close to one-third of all the cultivated land, to 800,000 tenants comprising, with dependents, some 40 percent of the rural population. The program virtually abolished land tenancy in Viet Nam. It raised the living standards of the farmer 30-50 percent and was responsible for a major share of the investment in agriculture that was so noticeable during these years. Compensation to former landlords totaled VN\$201 billion in cash and bonds.

206

L. Exports

Exports were the principal bright spot during 1973 and, at least, by comparison with the rest of the economy, in 1974. Helped by strongly rising prices for rubber, shrimp, and pine logs, export earnings increased from \$23 million in 1972 to \$60 million in 1973. World demand for Viet Nam's principal exports continued strong through the first quarter of 1974, but then slackened and the export trend was flat thereafter. Total earnings for all of 1974 were \$75 million, a disappointment in view of earlier hopes for \$100 million. A hopeful sign in 1974 was the progress made by exporters of manufactured goods, notably handicrafts, finished plywood and furniture. The most important exports in 1974, ranked in order of earnings, were as follows:

	(\$ Millions)	
	<u>1973</u>	<u>1974</u>
Frozen shrimp	12.7	24.5
Rubber	12.7	14.4
Forestry products	12.1	10.2
Fish products (except shrimp)	1.2	4.9
Coffee	1.8	4.5
Handicrafts	1.0	2.6
Non-ferrous scrap	5.5	1.8
Tea	0.6	1.2
Duck feathers	1.3	0.9
Cinnamon	0.9	0.7
Other	<u>10.6</u>	<u>9.3</u>
Total	60.4	75.0

M. Foreign Investment

With the 1972 NVA offensive, most major prospects for foreign investment evaporated. The Paris agreement and cease-fire did little to ease the fears of investors. Absence of OPIC guarantees for American investors, and a similar lack of guarantees for Japanese investors, con-

tributed to the constraints in 1973. Another less recognized factor inhibiting foreign investment in the 1970's was the array of bureaucratic obstacles confronting potential investors. Regardless of the wording of the liberal Foreign Investment Law, and the undoubted good intentions of top level GVN officials, Viet Nam remained ensnared in red tape and delay at the lower levels of government. Countless stories of potential investors having to get scores of separate approvals from lethargic, sometimes hostile, officials located all over Saigon, attest to the foregoing. In an effort to solve the problem, the GVN in 1974 initiated a "one-stop investment service," which was supposed to place in one building representatives of all ministries charged with passing on investment proposals. It soon developed that the representatives assigned to the "one-stop service" were not vested with final approval authority and were merely referring proposals back to their ministries. By the time this problem was ironed out, it was too late in the day to do very much for foreign investment.

(1) 1973

No major investments were made, although a trickle of small investments continued. A total of \$22.6 million in 55 projects from 14 countries received GVN approval in 1973, of which only a few were to reach the implementation stage. The principal development in 1973 was the start of oil exploration off Viet Nam's east coast. Bidding for leases, postponed at the time of the 1972 offensive, was held in July 1973 and resulted in lease contracts with four foreign groups. Some \$17 million was paid over in signature bonuses in September.

(2) 1974

Offshore oil exploration accounted for much of the activity and most of the excitement in 1974. Quantities of oil were found in two test wells in August and September. Both wells were capped and drilling was begun in neighboring areas to determine whether oil existed in commercially exploitable quantities. The oil companies paid \$30 million to Viet Nam in exploration fees during 1974.

Concluding more than two years of off-and-on negotiations, the French government, several banks, and Polysius (an equipment supplier) agreed in December 1974 to finance a \$40 million expansion of Viet Nam's Ha Tien cement facility. The project was to expand Viet Nam's cement output by 70,000 tons annually, bringing production to 80 percent of the country's cement requirement. On the debit side, negotiations with Hyatt International Hotels for construction of a luxury hotel in Saigon were postponed indefinitely in November when company officials and the government failed to agree on tax considerations after two years of trying negotiations.

Apart from these major developments, new investments in 1974 consisted of a number of small firms, mostly in labor intensive, light manufacturing projects. A total of 66 projects valued at \$6.9 million received approval.

There were a number of promising institutional developments in 1974. OPIC guarantees for American investors were reinstated on August 17; the Export-Import Bank revised past policy and agreed to consider financing proposals; and the GVN decreed establishment of Viet Nam's first Export

Processing Zone on May 19. Some six firms applied for OPIC coverage. One loan application was submitted to the Ex-Im Bank to finance equipment for the Export Processing Zone and a project to build an earth satellite ground station was to be submitted in the future. The EPZ, located in the Saigon port area, contracted with seven tenants and three were installing their equipment in 1974. The projects, all joint ventures with Vietnamese and foreign capital, were to produce garments, knitware, work gloves and furniture.

N. Income and Employment

GVN national account statistics show virtually no change in GNP from 1971 to 1974, which would translate to a per capita decline of eight percent. Very likely the data err on the high side, especially with respect to 1974 where it seems certain that the sharp declines in manufacturing, forestry, and fishing more than offset the gain in crop output. Moreover, goods availability, or consumption, certainly lagged behind GNP, inasmuch as the latter was maintained by a continued growth in the public sector. Mission economists estimated the per capita decline in private consumption at from 15 to 20 percent during this period.

The impact of the decline was most heavily felt in the urban areas. In fact, it appears on the whole that income levels were maintained, perhaps even improved somewhat, in the agricultural areas. Even this statement needs qualification, since, unquestionably, the Delta farmer did better than the farmer in central Viet Nam. Assuming, though, that farm incomes on the average held unchanged during 1971-74 and that the 42 percent of the population classified as urban suffered all of the country-wide decline in income, the fall in per capita urban incomes

alone had to be one of 36 to 48 percent.\* This statistic was borne out by the countless stories of individual hardship, as well as by the undoubted steep rise in unemployment.

Data on unemployment in Viet Nam were unavailable. In an effort to satisfy the foreign press, which seemingly could not believe the figures were not there, Mission economists used a rule of thumb calculation to show that unemployment by the end of 1974 had to be a minimum of 1.2 million. In arriving at this figure, it was assumed that full employment, except in the frictional sense, existed in 1971. That provided a "basic" unemployment figure of 230,000 (.03 times the 1971 labor force, estimated at 7.8 million). It was assumed that there was no net job creation during 1971-74, the roughly 30,000 new jobs in government plus any new jobs in agriculture being offset by jobs lost in industry. To the base figure of 230,000, one then added the natural increment to the labor force and the 300,000 either discharged from U.S. sector employment or indirectly unemployed as a result of the U.S. withdrawal, and subtracted the annual draft of males to replace military losses:

Basic unemployment, 1971-74	230,000
Labor force increment, 1971-74	850,000
Decline in U.S. sector employment	<u>300,000</u>
Subtotal	1,380,000
Less: Military replacement	<u>-180,000</u>
Estimated unemployment, 1974	1,200,000

The estimated 1.2 million unemployed was equivalent to 14 percent of the labor force or, since virtually all of the unemployment existed in

---

\* a)  $.58 + (.42 \times .52) = .8$   
b)  $.58 + (.42 \times .64) = .85$

21

the cities, one-third of the urban labor force.

O. Money Supply and Inflation

(1) 1973

Money supply increased in 1973 by VN\$40.3 billion, or 17.7 percent; more broadly defined to include savings deposits, the increase was one of VN\$74 billion, or 26 percent. Many believed that the alternative, or  $M_2$ , definition of money supply had become necessary because of a tendency of savings deposits to become more liquid during 1973.

Whatever one's definition of money supply, its increase was far outstripped by the rate of inflation, which reached 62.5 percent. \* Two-thirds of the 1973 increase could be accounted for by the higher prices of imported goods within the price index, and the doubling of domestic rice prices discussed above. Prices of imported goods were propelled both by the world-wide commodity price inflation, which in the case of Viet Nam's inflation amounted to 50 percent during the year, and to the continuing piaster devaluation. During 1973 the GVN import rate was devalued by 18 percent, the CIP rate by 45 percent, for an average devaluation \*\* of 31 percent. Allowing, then, only for exchange rate devaluation and dollar import costs, average piaster import costs rose during 1973 by 96 percent ( $1.31 \times 1.50 = 1.96$ ). With import tax increases and advance deposit costs added, the increase would be seen as over 100 percent.

(2) 1974

---

\* NIS Working Class Index, without rent. The more widely quoted USAID index rose 65 percent. This paper has adhered to the broader-based NIS index throughout.

\*\* Average weighted by values of GVN and CIP imports in 1972: \$249 million and \$284 million, respectively. PL 480 imports omitted as some were subject to the GVN rate, some to the CIP rate.

World-wide inflation got a fresh boost with the 150 percent rise in POL prices decreed by the OPEC countries in November and December 1973 and, as was noted in Section G(2) above, the GVN passed on all of the increase, and then some, in pump prices. With this as stimulus, consumer prices rose 21 percent in the first quarter of 1974, an annual rate of over 100 percent. At that point, the world-wide inflation slackened to an annual rate of about ten percent and Viet Nam's inflation subsided to a 'normal' Vietnamese pace. Prices for all of 1974 rose by 37 percent (on the USAID index; NIS index not available for all of 1974).

Money supply in 1974 increased by VN\$65.9 billion, or 24.6 percent.  $M_2$ , or money supply defined to include savings deposits, rose by 33.3 percent. By either definition, the increase in money supply again trailed the rate of price inflation.

P. Banking and Credit

(1) Credit -

GVN policy with respect to credit was to accord maximum priority to development lending, primarily through the development banks (IDB and IDEBANK for industry and ADEV for agriculture), meanwhile keeping a tight rein on credit for other purposes. Importers continued to claim a large share of credit expansion as, whatever their real value, the piaster value of imports continued to rise strongly; nevertheless, in 1974 net credit extended by the development banks for the first time exceeded the amount of credit extended by the commercial banks.

213-

Net Credit Extensions 1972-74  
(VN\$ Billions)

	<u>Credit Outstanding Year-End</u>			<u>Year-to-Year Increase</u>	
	<u>1972</u>	<u>1973</u>	<u>1974</u>	<u>1972-73</u>	<u>1973-74</u>
Commercial Banks	83.6	149.7	186.5	61.1	36.8
Development Banks	22.0	40.1	82.5	18.1	42.4
(Industrial Banks)	( 6.5)	(10.3)	(20.0)	( 3.8)	( 9.7)
(ADB & Rural Banks)	(15.5)	(29.8)	(62.5)	(14.3)	(32.7)

Credit policy was not as restrictive in 1974 as the data above would imply; there was a VN \$43.2 billion decline in advance deposits outstanding that served to ease the situation. Moreover, to the extent firms were having difficulty obtaining credit--and there is no question that they were--the competing attractiveness of Treasury Bills--at no risk to the banks--was probably more of a factor than credit restraint per se (see Section (3) below).

(2) Savings

The tendency of savings deposits to become more liquid was accompanied by a levelling off in fixed term deposits after the first quarter of 1973. The increasingly negative interest rate was, at least, partly responsible, as time deposits rose by only VN\$ 1.4 billion for the full year. The closing of the Tinh Nghia Bank, Viet Nam's second largest, as a result of corruption charges levied on its president, produced a lessening of confidence in the banking system and was also at least a temporary factor in the levelling off in time deposits. Time deposits began to move upward again in 1974, especially later in the year as the inflation rate slowed. Treasury bond holdings of individuals roughly doubled in both years, reaching VN\$ 44 billion at the end of

244

1974.

Together, time deposits and Treasury Bond holdings of individuals rose by VN\$ 61 billion during 1973-74 and were a vital factor in limiting the increase in money supply.

(VN \$ Billions)

	Outstanding, Year-End			Increase
	1972	1973	1974	1972-74
1) $M_1$ (Demand deposits & Currency)	227.8	268.1	334.0	106.2
2) Savings deposits	58.5	92.2	152.2	93.7
3) $M_2$ ( $M_1$ + savings dep.)	286.3	360.3	486.2	199.9
4) Time deposits	57.9	59.3	87.3	29.4
5) Treasury bond holdings of individuals	12.5	24.0	44.0	31.5
6) Time deposits plus Treasury Bill holdings	70.4	83.3	131.3	60.9
7) $M_2$ ( $M_2$ +6)	356.7	443.6	617.5	260.8
8) (6) as % $M_2$				23.3%

### (3) Interest Rate Policy

GVN interest rate policy was the subject of considerable debate, especially in 1974. The debate was on the overall rate level, the subsidiary question of Treasury Bill rates, and the level of development lending rates in general.

#### a. Overall Rate Level

The mission began urging the GVN to raise interest rates in 1973, mainly to encourage term savings which had stopped rising early in the year, but also as a check to lending activity in general. The move was strongly resisted by influential Cabinet members, including the Finance Minister, and nothing was done. By early 1974 most observers seemed to feel that in view of the deepening recession an increase in interest rates was no longer desirable. The debate had, however, acquired a life

215

of its own and, in July, those in favor finally prevailed. Interest rates were raised by two to three points across the board, producing a prime lending rate--after the value added tax and miscellaneous banking charges--of 35 percent.

The July increase seemed from the start to have been a mistake; there was a strong cry of protest in business circles. USAID advisors urged that the rate be lowered but, above all, kept flexible. There was no retreat and, meanwhile, the issue became mixed up with the question of interest rates on Treasury Bills.

b. Treasury Bill Rates

Treasury Bill rates, at 19 percent, were well below the prime lending rate of 26 percent but, as earnings on Treasury Bills were tax exempt, the larger, profitable banks could do better buying bills than making business loans. Bank purchases of Treasury Bills had been encouraged to provide an outlet for the increased savings of individuals in the wake of the 1970-71 reforms, and the policy had worked well. In the hazardous business climate of 1974, however, it appeared too much of a good thing. Bank holdings of Treasury Bills more than doubled in 1974, rising from VN\$ 68 billion to VN\$ 140 billion. The VN\$ 72 billion increase contrasted with an increase in commercial loans outstanding of only VN\$ 37 billion, and the relative attractiveness of Treasury Bills was generally recognized as a factor in the deepening recession.

The recommended solution was elimination of the tax exempt feature along with a moderate increase in Bill rates to retain an appropriate incentive for the banks to encourage savings deposits. After prolonged debate on the appropriate move, the GVN/eliminated the tax exemption on January 1, 1975

2/6

feature on Treasury Bills and lowered bank lending rates by two percent, but they neglected to adjust Treasury Bill interest rates. The result appeared to be the worst of both worlds. Bank loans remained unattractive to the bankers, and now Treasury Bill rates were too low--so the bankers alleged--to cover the interest they had to pay on deposits. One undesirable result was that many banks began turning away, or limiting, new savings deposits, a situation that was to prevail to the end.

C. Development Lending

Lending rates of the two industrial development banks were set at 15 percent for the obvious reason--to encourage development lending. The policy was successful in its immediate goal, as these institutions had no trouble lending up to the limit of their capital availabilities. However, the low lending rate encouraged speculative projects, especially where the borrower had access to import funding. The issue had not been explored in depth by the time Saigon fell.

Agricultural lending rates were set roughly at par with those of the commercial banks. Demand was strong and there was a good economic case for letting the rate move upward. The banking system accounted for only a very small share of total agricultural credit--perhaps 20 percent--the remainder being supplied from traditional sources (merchants, money lenders, etc.) at rates up to 60 percent or more. If the ADB and rural banks could raise their rates, they could presumably raise more--eventually all--of their capital from savings, thus doing away with inflationary budget advances. Agricultural lending rates on the whole would be brought down, even though bank rates would rise. An offshoot

217

of the argument held that the ADB was so inefficient—in fact, it was a deficit operation even with interest-free GVN advances—that it should be required to earn its own way one way or another.

The argument encountered the flat refusal of the Ministry of Agriculture to countenance higher lending rates, and there were few willing to contest the issue in the difficult political climate then prevailing.

Q. GVN Expenditures

(1) 1973

GVN expenditure during 1973 totaled VN\$ 515 billion, including VN\$ 38 billion for the Relief, Rehabilitation and Reconstruction program announced in July (see Section T below), compared with 1972 expenditures of VN\$ 366 billion. This represented an increase of about 41 percent. Since the year-to-year increase in prices was on the order of 45 percent, GVN expenditures declined slightly in real terms from 1972 to 1973. During 1973, wages of GVN civil and military employees were raised only once, by a flat VN\$ 3,000 per month, effective September 1. The average increase in payroll cost of this raise was only about 17 percent. It is, thus, apparent that the GVN's soldiers and civil servants again bore a major share of the real burden of inflation in 1973. Defense continued to be the main budget expense, taking about VN\$ 283 billion; or 55 percent of total expenditures in 1973, compared to VN\$ 233 billion, or 64 percent, in 1972. Defense costs were still dominated by the expense of maintaining forces in being, and the total GVN force level was not altered appreciably in 1973.

(2) 1974

218

GVN expenditures in 1974 totaled VN\$ 720 billion, an increase of 40 percent over 1973. Expenditures under the Relief, Rehabilitation, and Reconstruction program amounted to VN\$ 50 billion. Security-related expenditures (MOND and Police) declined as a percent of the total, from 55 percent in 1973 to 48 percent in 1974. About VN\$ 70 billion of the total represented net financing of NFA rice operations, half for the rice subsidy and half for stock buildup and miscellaneous expenditures. Export and fertilizer subsidies cost another VN\$ 15 billion between them.

In an effort to deal with rising unemployment, the government expanded its short-term work programs. In the Saigon area 7,000 people were employed in public service projects similar to the successful Da Nang effort (Agency for Development of the Da Nang Area, or ADDA) that began in 1971. By year's end, total employment in job programs had reached 25,000 throughout Military Regions 1, 2, and 3. The government was planning further expansion in 1975, with emphasis on small labor-intensive development projects.

R. GVN Revenues

(1) 1973-74 Results

Domestic tax revenues rose dramatically in 1973 and through the first quarter of 1974. The 1973 increase was one of 93 percent, which translated to a real increase of 33 percent after allowance for a 45 percent rise in average prices between the two years. After the first quarter of 1974, revenues flattened out, reflecting the severe recession and consequent erosion of the tax base. It appeared also that the impetus given to tax revenues by the 1972 tax measures and by the inaugura-

tion of the Value Added Tax in July 1973 had been largely spent. Domestic revenues for all of 1974 totaled VN\$ 296 billion, a 53 percent increase over the VN\$ 193 billion collected in 1973. The 1974 performance represented a six percent decline in real terms.

Import revenues were little changed during 1972-74. A declining proportion of highly taxed luxury imports offset the effect of a rising piaster value of imports.

<u>Tax Revenues</u>	<u>(VN\$ Billions)</u>			<u>(Year-to Year % Increase)</u>	
	<u>1972</u>	<u>1973</u>	<u>1974</u>	<u>1972-73</u>	<u>1973-74</u>
Domestic	100	193	296	93	53
Foreign	<u>47</u>	<u>53</u>	<u>47</u>	<u>13</u>	<u>(11)</u>
Total	147	246	343	68	39

(2) Value Added Tax

The most important development in the revenue area during this period was the introduction of the Value Added Tax (VAT). Announced by Presidential decree in 1972, it had originally been scheduled for implementation on January 1, 1973, but was postponed owing to technical problems and the absence of any public information program at the time. Unfortunately, there was still no public information program when the VAT was finally launched on July 1, 1973. VAT, in its initial form, applied to transactions down to the retail level, including the smallest of firms ("anything not on wheels" was the Finance Ministry's intention). It was a highly sophisticated tax with a history of difficult implementation even in Europe. Not surprisingly, it proved utterly confusing to the small Vietnamese merchants, most of whom failed to comprehend the "value added" aspect of the tax and simply tacked ten percent onto their

220

prices. Prices shot upward across the country in reaction to the VAT and there was a public outcry reminiscent of the reaction to the austerity tax measure of October 1969. After much agonizing, the GVN finally backed down and, on August 9, rescinded that portion of VAT that applied to retail trade. It was left intact for imports and at the wholesale level.

While VAT probably did not have a permanent effect on the rate of inflation, it did aggravate the economic situation in 1973 and, perhaps most unfortunate, was an important factor, at least, in the resignation of Finance Minister Trung, along with Economy Minister Ngoc, in October 1973. For all of that, the VAT became Viet Nam's biggest single revenue producer. It was a crucial factor in the Directorate General of Taxation performance during 1973-74, which, by any reckoning, was one of the leading success stories of the U.S. involvement.

S. Deficit Financing

Domestic revenues accounted for 41 percent of GVN expenditures in 1974 as compared with 27 percent in 1972 and only 19 percent in 1971. Nevertheless, the deficit, before foreign aid, remained at 52 percent of expenditures. The following table shows the development of the deficit during 1972-74 and its financing. Noteworthy is the sharp increase in the share of financing accounted for by Treasury Bond sales in 1974.

	1972	1973	1974
	(VN\$ 3 millions)		
<u>a. Calculation of deficit</u>			
Expenditures	366	515	720
Revenues	147	246	343
(Domestic)	(100 )	(193 )	(296 )
(Foreign)	( 47 )	( 53 )	( 47 )
Deficit before foreign aid	219	269	377
(Domestic revs. as % exp.)	( 27.3)	( 37.5)	( 41.1)
(Deficit as % exp.)	( 59.8)	( 52.2)	( 52.4)
<u>b. Financing of the deficit</u>			
Counterpart	109	133	258
NEVK advances	-28	85	29
Treasury bonds	37	18	90
Revaluation profits	61	-	-
• Other (adjustments)	40	33	-

T. Economic Development

Until the 1970's economic development took second place to stabilization and the effort to control inflation. Development took place but did so through the workings of a market economy and not as a formalized effort. The principal planning exercise was the work during 1967-69 of the Postwar Planning Group, a joint effort of the Development Resources Corporation headed by David Lilienthal, and a staff of Vietnamese economists under Professor Vu Quoc Thuc. The group's studies culminated in some 60 papers and studies, the most important of which was the 3-volume work, "The Postwar Development of Viet Nam; Policies and Programs." The GVN did not make a serious effort to follow-up on the proposals for further work made in this study.

The existing planning agency was upgraded from Directorate General to Ministry status with the formal establishment of the Ministry of Planning in June 1971. The activities of the new Ministry centered on the production of a 1972-76 Five Year Plan, which was presented to President Thieu in the summer of 1972 and received his formal approval in November of that year. Unfortunately, events in the form of the NVA offensive had overtaken the planners. While rated a good job in terms of internal consistency and logic, the plan was unrealistic, having failed to account for a bad year right at the start. It would become more so as real aid levels declined during 1971-74.

Meanwhile, a number of more practical developments had been taking place. A new liberal, Foreign Investment Law was promulgated in 1972. An Export Development Center and an Investment Service Center were established. The National Economic Development Fund (NEDF) was started on

March 1, 1972 to provide medium and long-term credit to business through development banks and other financial intermediaries. The activities of the Agricultural Development Bank (ADB) and rural banking system expanded and received official encouragement. The Handicraft Development Center was revived. In general, the new institutions were capably staffed and, despite early difficulties, performed usefully.

In May 1973, as a follow-up to his meeting with President Nixon at San Clemente, President Thieu proclaimed an "Economic and Social Reconstruction Program," designed to restore the damage done by the 1972 NVA offensive, complete the Refugee Resettlement Program, and lead the country to self-sufficiency by 1980. A VN\$150 billion piaster "Reconstruction, Rehabilitation, and Redevelopment Fund" was established as an extrabudgetary fund to finance activities in the areas named. Foreign donors were invited to finance the new "3-R" Fund.

Curiously, the 1973-80 program and the 3-R Fund originated not in the Ministry of Planning but at the Ministry of Finance, which received Presidential approval as the coordinating body for all foreign aid.

The Planning Ministry in 1973 was being pressed by USAID to move away from its penchant for formal macro-economic planning into identification of actual projects. To that end a "shelf" of projects, intended as a focus for potential foreign lenders, was produced in mid-1973. The list was not well conceived, and despite further efforts, the GVN never was able to produce a truly creditable, carefully costed listing of well defined development projects.

Spending under the 3-R program lagged far behind the initial VN\$150 billion figure, totaling VN\$38 billion in 1973 and about VN\$50 billion in 1974.

224

Most of it was for refugee relief. Of the remainder, the Agency for the Development of Da Nang Authority (ADDA) took a major share. ADDA was established in 1971 to provide public works employment in the wake of the U.S. withdrawal. Capably managed, it soon attained a rare reputation for honesty, and steadily expanded its scope, both in area and in the nature of its operations. By the end of 1974 ADDA was active in several of the larger cities in Central Viet Nam and a sister agency, ADSA, had been formed in Saigon. ADDA's activities had expanded from street cleaning and repair of streets and buildings to large scale irrigation projects. It had, in effect, evolved into the GVN's principal operating agency in the area of development, employing 25,000 persons in Central Viet Nam and 7,000 in Saigon (ADSA).

In August 1973 the Planning Ministry was downgraded to Commissioner General status. There followed a period of confusion in which the role of the Commissariat General was never fully clarified. Full Ministry status was restored in March 1974, but the change brought no significant increase in effectiveness. Except for ADDA, which was independent of the Commissioner General of Planning in any case, the GVN was unable to conceive, organize, and carry through on specific development projects. Near the end, their ineffectiveness in this area became moot, at least in many minds, as the deteriorating monetary outlook brought into increasing question the advisability of such projects.

U. Exchange Rate Policy

The GVN's basic policy in the area of exchange was to continue the "trotting peg" method of devaluation at a rate sufficient to maintain the international parity of the piaster. Subsidiary policies were to

225

narrow the differential between the GVN and CIP import rates and to provide an incentive rate for exports.

1. Official Rate

The Official Rate was changed in 18 separate steps from 465 at the end of 1972 to 685 at the end of 1974, an overall move of 47 percent. There was a continuous, often heated, debate on the question as to whether, in fact, the rate of devaluation was sufficient to maintain the parity of the piaster. Doubters pointed to the 127 percent increase in prices in Viet Nam during 1973-74 and maintained that a 47 percent piaster devaluation was insufficient to cover the difference between this rate and the rate of inflation in the rest of the world. The Mission, whose measurements of the situation differed from the others (especially AID/Washington), felt that the devaluation was sufficient and that, moreover, a higher rate of devaluation had to be ruled out on grounds of domestic economic considerations. At this point, the argument broadened to cover economic policy as a whole (see Section V below).

2. GVN-CIP Differential

The CIP rate was adjusted from 320 at the end of 1972, at which point it was 145 piasters below the GVN rate, to 465 on January 4, 1974, by which time the differential was 95 piasters. On January 14, 1974 the CIP rate, as such, was dropped; henceforth, importers of CIP goods were subject to the GVN rate, but received a rebate after their goods' clearance through customs. The rebate was initially set at 85 piasters to the dollar; it was adjusted to 60 in March 1974, where it remained to the end. By the end of 1974 the effective differential was 9.2 percent measured on

the CIP rate, which compares with 45.3 percent at the end of 1972 and 45.5 percent at the end of 1971.

The principal reason for the narrowing of the differential and its eventual removal in favor of a rebate system was IMF disapproval of the existence of a multiple rate system. A contributing factor was the GVN's desire not to appear to favor American suppliers over those from other countries whose aid they were soliciting. Economically the narrowing of the differential could be justified to some extent by the ongoing devaluation of the dollar vis-a-vis other world currencies during most of this period. Nevertheless, CIP goods on the whole became increasingly expensive relative to GVN goods during 1973-74.

### 3. Export Rate

Between May 1972 and January 1974 the GVN maintained a preferential export rate involving a premium on the Official Rate that fluctuated between 28 percent at the high and 2.6 percent at the low. The export rate was pegged at 575 from January 1973 to January 1974 while the Official Rate rose, resulting in the progressive narrowing of the premium. At that point, the system was changed, again at IMF urging, so that instead of a separate export rate, exporters received an "interest rate premium" intended to compensate them for the cost of financing. In effect, this amounted initially to a subsidy of 6.5 percent. The subsidy was changed to an effective 13 percent in March 1974, but only for the fisheries, forestry, tea and rubber industries. In December 1974 the subsidy was modified again: to 10 percent generally, but 15 percent for a number of industries deemed to have been hurt by the fuel crisis.

The GVN was constrained in its export rate policy by the consideration that too high a rate would encourage overinvoicing, and there was evidence to the effect that overinvoicing was taking place. Mission economists were less concerned about overinvoicing since the dollars would have to be converted legally, whether as exports or concealed capital inflow, the principal damage being to the reliability of export statistics.

More important, the "interest rate subsidy," together with the GVN's constant juggling of eligibility criteria, proved a major source of confusion to exporters. Many did not understand the concept to begin with; no one could be sure what he would be entitled to by the time his transaction was completed. While the Export Development Center did its best, top level economic officials never developed a meaningful export drive and the Ministry of Finance was more concerned for the budgetary effect of an export subsidy than it was for export development.

V. The Great Debate; Monetary vs. Cost Inflation

Economic policy in 1973-75 was marked by a continuous, often heated, debate on the nature of Viet Nam's inflation problem and the appropriate remedies. The lines of opinion were not always clearly drawn, especially as the focus of the debate itself shifted, but at the risk of oversimplification, certain positions can be stated.

The Mission, among others, believed that the inflation of 1973-74 was caused primarily by the worldwide commodity price inflation and resultant surge in Viet Nam's import costs together with the decline in goods availability--both from production and from imports--that was taking place. The IMF, among others, argued that the inflation was inspired primarily by excessive demand and pointed to rising budget deficits.

Shadings of opinion appeared when it came to remedies. On the one hand, Professor Arthur Smithies of Harvard, an advisor on the Vietnamese economy of long-standing, believed that the rapid piaster devaluation of 1973, taken together with the policy of monetary restraint, was a primary factor in the recession of 1973-74<sup>a/</sup> His views were largely echoed by Albert Williams and John Kohler of the Rand Corporation, who issued their own study in November 1974<sup>b/</sup> Williams and Kohler contended that devaluations should be held to a minimum and that the GVN should explore alternative means to encourage exports. At the other extreme, the IMF argued that much more rapid devaluation, much higher interest rates and tighter restraint on GVN spending were essential if the GVN were ever to break away from its dependence on imports and achieve self-sufficiency. Their

a/ Arthur E. Smithies, "Inflation and Depression in Vietnam, 1973-74."

b/ John E. Kohler and Albert P. Williams, Jr., Rand Corporation Nov., 1974 - The Vietnamese Economy in October 1974 - An Assessment with Policy Recommendations.

229

view had support in the undeniably grim monetary outlook in prospect for 1975.

The Mission's position was somewhere in between, albeit closer to Smithies, Williams and Kohler. They agreed with Smithies as to the depressing effect of devaluation in 1973, but believed it had been essential, nevertheless, in order to maintain international currency parity. They disagreed with the IMF prescription, feeling: (a) the GVN was devaluating as rapidly as it needed on a parity basis, and more rapid devaluation would serve only to increase the unemployment roll; (b) higher interest rates would topple many companies caught with high inventories and already on the brink; and (c) given the military imperative, there was very little to cut out of the budget (nor did the IMF offer any specific suggestions).

Both sides to the argument favored productive development and prodded the GVN to undertake the kind of labor-intensive, high yield projects, the feasibility of which was already being demonstrated by ADDA. Here, however, the agreed direction encountered the seeming paralysis of GVN economic leadership and their plain inability to get development projects off the ground. Later, in 1975, even their development efforts would come to be questioned for their inflationary impact.

W. GVN Economic Organization

The deterioration in the economic situation during 1972-73 brought general discredit to the architects of the liberal reforms of 1970-71, even though the country's miseries were the result of external circumstances beyond their control. They were blamed, in particular, for the high level inflation of 1973 and, after the particularly sharp increase in rice prices in the summer of 1973, advocates of direct controls were able to effect a substantial government take over of the country's rice pricing and distribution system. Shortly thereafter, Economy Minister Ngoc, who had resisted the control measures, was forced from office. With him went Finance Minister Trung, in discredit since the initial fiasco of the Value Added Tax (see Section R.2 above).

In the cabinet shake-up of October 1973, Ngoc was shifted to a downgraded Commissariat-General of Planning. His place at the Ministry of Economy, renamed the Ministry of Trade and Industry, was taken by his capable but youthful former deputy, Nguyen Duc Cuong. Trung left public office altogether and was replaced as Finance Minister by Chau Kim Nhan, a former accountant and auditor with the Ministry of Defense, who had a reputation for honesty but little experience in economic policy.

Apart from marking the ascendancy of control-minded, as opposed to liberal economic officials, the October 1973 shake-up left Viet Nam without economic leadership. Viet Nam had not had a formal super-minister of economics and now the pro forma leadership previously exercised by Ngoc was gone (though he did not give up without a battle). The lack of leadership came to be regarded as an extremely serious matter. With the

cabinet sharply divided on most issues, it became difficult to get action on important measures. When action was taken, it was liable to be so late that circumstances were already dictating an alternative course, as with the interest rate increase of July 1974. Exchange rate changes continued to take place, but even these were subject to delays. Action on foreign investment proposals was especially subject to delay, to the country's considerable cost.

A solution to the leadership problem was finally attempted with the appointment as "Super-Minister" of Dr. Nguyen Van Hao in November 1974. Dr. Hao was given the title of Deputy Prime Minister for Economic Development and, concurrently, Minister of Agriculture and Industry. The Ministry of Trade and Industry was renamed the Ministry of Trade and Supply and shorn of its Industry function. Replacing Cuong as the new Minister was a relatively obscure banker named Dung. Chau Kim Nhan resigned and was replaced by an equally obscure assistant from his own Ministry named Truong. Holdovers were National Bank Governor, Le Quang Vy, and Nguyen Tien Huong at an upgraded Ministry of Planning.

It can be said that the new cabinet was less liberal and generally less competent than the old. Most important, the appointment of Dr. Hao failed to resolve the leadership problem. A controversial figure as Director of NEDF, he had difficulty lining up support for his policies (which were not subject to easy definition) and it very soon became evident that nothing had changed. Whatever the form of the new organization, decisions were still taken only after much debate and, presumably, by majority vote. The situation did not auger well for the future.

XII THE END; 1975

A. Economic Events, January-March

The early months of 1975 saw a continuation of the trends under way since the first quarter of 1974. The recession in industry continued unabated. Manufacturing activity continued a gradual decline and unemployment moved inexorably upward. The rice crop appeared to be slightly better than that of 1973-74, and other crops were doing well. However, security problems were proving increasingly difficult in forestry, and the fishing industry was still hamstrung by high costs. Price inflation was proceeding at an annual rate of about 25 percent. With the budget deficit expanding rapidly and continuing pressure from the ongoing piaster devaluation, one might have expected more; it appeared that decreased consumer demand, even for essential foodstuffs, was the principal factor acting to moderate price increases. Relative quiet prevailed in the currency markets even after the fall of Phuoc Long Province in February. The black market rate for \$10 green was 785 in mid-March compared with 795 at the end of 1974, notwithstanding a rise in the official rate from 685 to 725 during the same period. Not until the fall of Ban Me Thuot on March 10 did the rate begin to move upward, reaching 880 at the end of March.

On the foreign trade front, exports continued the flat trend underway since the first quarter of 1974 and import demand declined to about half the reduced 1974 level. Foreign exchange reserves (gold, foreign exchange, and SDRs), which had peaked at \$228 million in November 1974, were declining steadily, reaching \$179 million on March 31. The balance of payments outlook was greatly worsened in the first quarter

233

by a number of disheartening developments, namely: an increasingly grim outlook for the FY 1975 A.I.D. appropriation; the prolonged debate over the \$300 million military Supplemental and consequent realization that even the remaining piaster purchase availabilities were in jeopardy; the decision by the IMF, in February, to exclude Viet Nam from eligibility for aid under the 1975 oil facility credits; and finally, the loss of the northern provinces, which brought sharply worsening prospects for exports and the possibility of capital flight instead of the inflow that the country had been enjoying.

B. The Fiscal Outlook

The 1975 GVN budget proposed in September 1974 called for spending of VN\$825 billion, which compared with actual 1974 expenditures of VN\$720 billion. Revenues were estimated at VN\$372 billion for a deficit of VN\$453 billion. After allowance for omitted items, including subsidies and a pay raise - which USAID at least considered inevitable - a more realistic estimate (i.e. USAID's final estimate) of 1975 spending was VN\$975 billion. If tax revenues were to be no more than the budgeted figure, the deficit before foreign aid would rise from VN\$377 billion in 1974 to VN\$600 billion in 1975. The money supply increase, based upon a budget deficit of this magnitude, was projected at upwards of 50 percent. The optimistic projections assumed a continuation of the savings trend of recent years, which by then was becoming very uncertain.

C. The Tax Dilemma

As noted, tax revenues, after rising spectacularly for two years, had levelled off after the first quarter of 1974. They were no longer

rising even in nominal terms. The problem did not lie with the tax administration. The problem was simply that the potential for further gain, given the existing tax structure, had been exhausted. A great deal of the tax base was import-oriented; this applied even to such nominally domestic taxes such as POL revenues. Of the remainder, the bulk of the revenues were accounted for by the sales of a handful of large, mostly foreign, companies in the beer, soft drink, and tobacco industries. By 1975 the effect of declining sales by these companies was at least offsetting the effect of any price increases on their products. Income tax revenues accounted for only 14 percent of domestic revenues; moreover, they were levied almost entirely on those least able to pay - the civil servants.

The one unquestioned source of significant new tax revenues was the rural economy. Despite significant progress made under the Local Revenue Improvement Program begun in 1971, rural tax revenues were only V\$4.2 billion in 1974, or 1.3 percent of all domestic taxes collected, national and rural. The farmer clearly could afford to pay more, especially in view of the Land Reform Program which had substantially increased his share of the national income, but there were well entrenched objections to taxing the farmer. The USAID Joint Economic Office was, nevertheless, readying a major effort to push a drastic increase in rural revenues when the crumbling military situation began to make it all seem academic.

D. The Monetary Trap Complete

The dimensions of a potential monetary disaster were becoming clear to all even before the fall of Phuoc Long. As long as the GVN had to

235

maintain a huge military force, expenditures would continue their rapid rate of increase. The domestic tax system had reached its existing potential and any new surge forward was a long term proposition, dependent on a basic restructuring of the tax system. In the past, it had been possible to call forth a surge of imports - or import taxes - to restrain inflation. Balance of payments realities made this impossible in 1975; in fact, the prospect was for declining imports. Finally, savings could not be counted on to continue rising as they had. In fact, economists were haunted by the prospect of dissaving. More rapid devaluation remained as a possible means of large scale increases in import absorption. However, devaluation was already at or near a rate at which the rate of devaluation itself triggers mass speculation and mission economists believed that the one large devaluation being recommended by the IMF - to perhaps 900 - would have a catastrophic effect on what was left of business activity.

It was always possible to be too pessimistic on the Vietnamese economy. Projections of runaway inflation in 1968, for example, had not been borne out. In 1975, however, there truly seemed nowhere left to turn. It would not be the first time that a country with great economic potential had foundered on the rock of financial instability and Viet Nam, with its endless war, had more reason to founder than most.

E. April

Just about all business activity came to a halt following President Thieu's order to evacuate Kontum and Pleiku on March 15. The collapse of the northern provinces followed shortly. Disaster was mirrored

- 226 -

in the progress of black market currency rates and gold rates. The rate for \$10 green was 1300 piasters on April 7, 2000 a week later, and near the end quotations of up to 5,000 were not uncommon.

The somewhat sick joke going the rounds in April was to the effect that Viet Nam was undergoing a surge in per capita GNP--a reference to the fact that the country no longer had to carry the burden of the less developed, poorer northern provinces. In fact, as late as mid-April Mission economists kept busy assessing the economic dimensions of the new truncated Viet Nam. To the extent their view could be divorced entirely from reality, they liked what they saw. They were not, however, to have long to ponder the matter.

#### XIV. A Footnote on Corruption

The subject of corruption has not heretofore been touched upon simply because there is no particular time frame in which it could be placed. Corruption was pervasive throughout the period of U.S. involvement at all levels.

Apologists for corruption in Viet Nam generally make one or more of the following observations: (1) it was not abnormal by the standards of Southeast Asia; (2) it was the "Asian way" of doing things and therefore not a matter for American concern--i.e., the "grease-the-wheel" theory according to which corruption is not harmful as long as it does not actually interfere with economic activity; (3) there was nothing the Americans could do about it anyway.

The third point may or may not be correct inasmuch as the extent to which Americans tried is unknown. But a dissent has to be entered on the

other two points.

Undoubtedly, Vietnamese officials had more opportunities for gains by corrupt means--the U. S. presence itself assured that--and more incentive to be corrupt than officials in other countries. At the lower levels of government, pay was so inadequate that the alternatives to bribe-taking were moonlighting, putting the family to work at menial tasks, or eating less. But there was an inordinate amount of corruption--by any standard.

Secondly, the amount of corruption was far beyond that which could be tolerated under the grease-the-wheel theory. Corruption involved an extensive interference with trade and commerce, enough to have been a key factor in the 1973-74 recession. The multiplicity of check points on roads and canals, especially, posed an increasing obstacle to commerce, and was an important factor in the high cost operations in export industries, such as fishing and forestry. At higher levels, corruption entered into dealings with prospective foreign investors and lenders. By 1973-74 matters had reached the point at which the fear of being accused of corruption was adding to the paralysis in economic decision-making by causing officials to shy away from sensitive areas - e.g., scrap and divestiture.

One could always understand the lower level official trying to make ends meet; to that extent corruption was mainly a result, rather than a cause, of the country's economic woes. What the people could not forgive was the repeated disclosures of corruption - often involving fantastically large amounts of money - among top officials and generals. Without wishing to downplay the effect of declining American aid and <sup>question</sup> is little / that corruption, especially high level corruption, was

critical factor in the deterioration of national morale which led ultimately to defeat.

XV. Conclusion

It seems clear to many observers, in retrospect, that the American advisors in the 1960s overrated the political dangers in high level inflation or, put another way, they underrated the toughness, the fortitude, of the ordinary Vietnamese citizen. The drastic decline in urban living standards of 1972-75 was the hardship equivalent of runaway inflation, yet there were no civil disorders and government institutions continued to function normally. In fact, most would agree that they functioned better than they had in the 1960s. The decision to protect the people from runaway inflation led to import levels in excess of economic need, with a consequent distortion of economic priorities and damage to the country's social structure and moral fabric. Most of all, it involved the creation of an artificial economy almost entirely dependent on U.S. aid and, of course, vulnerable to withdrawal of that aid.

The extent of the aid decline after 1971 can hardly be overstated. Nor can it be said that the reduced aid levels during 1972-74 merely returned the economy to a "normal" state of external dependence. U.S. import support in 1974 was 27 percent higher in real per capita terms than in 1964, i.e. before the start of full-scale U.S. involvement. Imports, similarly measured, were eight percent higher. However, the 1974 data were inflated by exceptionally large amounts of rice (which conveyed no lasting economic benefit) at vastly inflated prices. With rice omitted from the data, it is likely that neither U.S. import support nor actual imports

were higher on a real per capita basis than in 1964. If one considers that in the meantime the GVN armed forces had risen from 500,000 to 1.1 million men, it can be seen that both U.S. import support and the import level were far less adequate in 1974 than in 1964. As for living standards, per capita GNP in 1974 was five percent below the 1964 level, and the decline in per capita income was certainly greater than that. To be sure, declining real aid was partly the result of the worldwide inflation, but in fact, the U.S. did little to offset the impact of that inflation on the hard-hit Vietnamese economy.

South Viet Nam performed well in its initial efforts to adjust to the decline in aid levels. The sweeping reforms of 1970-71, the economic equivalent of Vietnamization, took place before the onset of the aid decline, and it is fortunate that they did. It is doubtful that the economy could have withstood the shock of the 1972-74 events, had the interest and exchange rate reforms, especially, not been in place. The tax performance of 1972-73 and the many institutional developments in 1971-72 also merit praise. Economic performance grew generally less commendable in the deteriorating situation after mid-1973, but by that time, events themselves had begun to take charge.

No one can say for certain, at least at this stage, to what extent, if any, the deteriorating economic situation contributed to the country's final collapse. Certainly military morale was affected both by inadequate pay and by the hardships being suffered by families at home. The effect of declining economic aid was not entirely separable from the more widely publicized reduction of military aid.

Table 1

U.S. Aid & Import Support, 1954-75  
(Obligations Basis - \$ Millions)

(1)	(2)		(3)	(4)	(5)	(6)	
Year <sup>a/</sup>	CIP <sup>b/</sup>	Food for Peace Title I Title II	Project & Other AID <sup>c/</sup>	Piaster Purchases <sup>d/</sup>	Total Aid (1+2+3+4)	Import Support (1+2+5) <sup>c/</sup>	
1954	-	-	0.1	-	1	0.1	1
1955	253.7	-	2.2	66.5	3	322.4	257
1956	174.7	-	14.3	21.0	3	210.0	178
1957	210.9	-	22.8	48.5	3	282.2	214
1958	151.9	4.4	5.2	27.5	3	189.0	159
1959	146.4	-	6.5	54.5	4	207.4	150
1960	135.6	5.0	6.3	34.9	5	181.8	145
1961	111.2	7.0	4.5	29.3	6	152.0	124
1962	94.1	26.8	5.1	30.0	7	156.0	128
1963	95.0	23.7	28.9	48.3	11	195.9	130
1964	113.0	34.3	24.8	52.7	15	224.8	162
1965	150.0	41.4	8.5	75.0	126	274.9	317
1966	399.3	98.2	44.8	194.2	333	736.5	830
1967	160.0	73.3	0.4	334.4	327	568.1	560
1968	160.1	96.6	41.9	238.1	301	536.7	558
1969	130.0	60.8	38.6	184.1	347	413.5	538
1970	238.5	75.6	35.2	127.4	318	476.7	632
1971	281.0	164.9	23.1	106.7	403	575.7	849
1972	313.0	62.5	5.3	73.8 <sup>e/</sup>	213	454.6	591
1973	226.2	179.0	9.3	87.2 <sup>e/</sup>	96	501.7	532
1974	335.1 <sup>f/</sup>	268.9	1.0	48.3 <sup>e/</sup>	97	653.3	727
1975	143.2	45.7	3.9	45.0	-	237.8	218 <sup>g/</sup>
Totals	4,022.9	1,268.1	332.7	1,927.4	2,622	2,551.1	8,000

Notes: (a) Fiscal years for all but piaster purchases, which are on a calendar year basis.

(b) Does not include deobligations.

(c) Including also Direct Dollar Support from 1972-75. See Note (e).

(d) Guesstimates for 1954-63; partially estimated for 1964-66.

(e) Broken down as follows:

	Humanitarian Aid		
	Project Aid	(Direct Dollar Support)	Total
FY 72	71.4	2.4	73.8
FY 73	56.2	31.0	87.2
FY 74	22.3	26.0	48.3
FY 75	15.7	29.3	45.0

(f) Includes Program Loan of \$50 million.

(g) Excluding piaster purchases of unknown amounts.

Sources: AID Statistics and Reports Division, "U.S. Overseas Loans and Grants" Viet Nam Program Summaries, AID Vietnamese balance of payments reports, National Bank of Vietnam MACV Piaster Expenditures Reports (from 1967)

241

Table 2

U.S. Import Support, Nominal and Real  
(1964-74)

	Import Support <sup>a/</sup> (\$ millions)	Import Price Index <sup>b/</sup>	Real Import Support (\$ 1964)	Support Index (1964=100)
1964	162	100.0	162	100
1965	317	102.0	311	192
1966	830	104.2	797	492
1967	560	106.2	527	325
1968	558	107.0	521	322
1969	538	110.5	487	301
1970	632	116.3	543	335
1971	849	119.9	708	437
1972	591	132.8	445	275
1973	532	179.3	297	183
1974	727	274.3	265	164

## Notes:

a/ Import Support defined as CIP, Food for Peace, Title I, Direct Dollar Support (Humanitarian Aid), and Piaster Purchases. CIP, FFP, and Direct Dollar Support on fiscal year basis, piaster purchases on calendar year basis (see Table 1).

b/ Mission calculation based on - 1964-71: IMF export price indexes of Viet Nam's leading suppliers. 1971-74: analysis of price changes of Viet Nam's principal import commodities, plus IMF export price indexes.

Table 3

Consumer Prices  
(Working Class Families in Saigon)

	Price Indices (1963=100)		Percent Increases	
	Annual Aves. <sup>a/</sup>	End of Year (a) (b)	Year to Year (a)	Dec. to Dec. (c)
1954	71.2	74.5		
1955	79.1	87.8	11.1	17.9
1956	89.5	83.0	13.1	-5.5
1957	85.0	83.8	-5.0	1.0
1958	83.1	84.2	-2.2	0.5
1959	85.4	83.9	2.8	-0.4
1960	84.3	87.3	-1.3	4.1
1961	90.1	91.3	6.9	4.6
1962	93.0	94.0	3.2	3.0
1963	100.0	100.0	7.5	6.4
1964	103.2	105.5	3.2	5.5
1965	122.5	143.4	18.7	35.9
1966	208.4	231.4	70.0	61.4
1967	305.6	335.8	46.6	32.0
1968	390.3	412.5	27.7	-22.8
1969	469.9	540.6	20.4	31.1
1970	640.0	715.4	36.2	32.3
1971	745.5	821.9	16.5	14.9
1972	941.1	1,047.9	26.2	27.5
1973	1,363.9	1,702.6	44.9	62.5
1974 <sup>d/</sup>	2,217.7	2,330.9	62.6	36.9

## Notes:

a/ NIS Working Class Index Excluding Rent

b/ NIS Working Class Index Including Rent

c/ 1955-67, including rent; 1968-73, excluding rent

d/ NIS data for 1974 not available. Index values obtained by applying increases in USAID retail price index to 1973 index values.

Source: National Bank of Vietnam; USAID.

Table 4

Money Supply and Prices  
(1957-74)

	Money Supply <sup>a/</sup>		Consumer Prices <sup>b/</sup> (% Inc. During Year)
	VN\$ Billions End of Year	Year to Year % Inc.	
1957	11.0		
1958	11.7	6.4	0.5
1959	14.1	20.5	-0.4
1960	16.8	19.1	4.1
1961	17.2	2.4	4.6
1962	19.5	13.4	3.0
1963	22.3	14.4	6.4
1964	27.4	22.9	5.5
1965	47.6	73.7	35.9
1966	63.5	33.4	61.4
1967	82.2	29.4	32.0
1968	124.1	51.0	22.8
1969	140.7	13.4	31.1
1970	162.9	15.8	32.3
1971	198.8 <sup>c/</sup>	22.0	14.9
1972	227.8	14.6	27.5
1973	268.1	17.7	62.5
1974	334.0	24.6	36.9

a/ Demand deposits and currency

b/ NIS Working Class Index: including rent through 1967;  
excluding rent 1968-74.

c/ Data adjusted to exclude VN\$ 9.6 billion of excess balances held  
by the U.S. Disbursing Officer at the end of the year.

Source: National Bank of Vietnam

- 244 -

Table 5

Money Supply and Savings 1967-74<sup>a/</sup>  
(VN\$ Billions)

End-Year	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
	Money Supply (M <sub>1</sub> ) <sup>b/</sup>	Private Sector Savings			Total (2+3+4)	Year-to-Year Increase		(7) as % (6+7)
		Savings Deposits	Term Deposits	Treasury Bond Holdings of Individuals		M <sub>1</sub>	Total Savings	
1967	82.2	2.6	1.9	0.1	4.6	-	-	-
1968	124.1	4.4	3.5	0.8	8.7	41.9	4.1	8.9
1969	140.7	5.8	8.1	1.5	15.4	16.6	6.9	29.4
1970	162.9	7.2	15.7	2.7	25.6	22.2	10.2	31.5
1971	198.8 <sup>c/</sup>	13.9	36.3	6.6	56.8	35.9	31.2	46.5
1972	227.8	58.5	57.9	12.5	128.9	29.0	72.1	71.3
1973	268.1	92.2	59.3	24.0	175.5	40.3	46.6	53.6
1974	334.0	152.1	87.3	47.1	286.5	65.9	111.0	62.7

a/ Saigon commercial banks only

b/ Demand deposits plus currency in circulation

c/ National Bank data adjusted to exclude VN \$9.6 billion of excess balances held by the U.S. Disbursing Officer at the year-end.

Sources: National Bank of Vietnam; U.S. Disbursing Officer, Saigon

Table 6

Credit, 1955-75  
(VN \$ Billions)

End-Year	Credit Outstanding, Year-End			Year-to-Year Increase	
	Commercial Banks <u>a/</u>	Development Banks <u>b/</u>	ADB <u>c/</u> / IDB & IDEBANK	Commercial Banks	Development Banks
1955	1.0	-	-		
1956	2.0	-	-	1.0	-
1957	3.2	-	-	1.2	-
1958	3.0	-	-	-0.2	-
1959	3.7	-	-	0.7	-
1960	4.3	-	-	0.6	-
1961	5.3	-	-	1.0	-
1962	6.5	-	-	1.2	-
1963	7.1	-	-	0.6	-
1964	7.2	-	-	0.1	-
1965	6.8	-	-	-0.4	-
1966	28.8	-	-	22.0	-
1967	28.9	-	-	0.1	-
1968	26.4	-	-	-2.5	-
1969	29.3	-	-	2.9	-
1970	42.1	5.5	3.8	12.8	-
1971	63.1	8.7	4.7	21.0	4.1
1972	88.6	15.5	6.5	25.5	8.6
1973	149.7	29.8	10.3	61.1	18.1
1974	186.5	62.5	20.0	36.8	42.4
Jan. 31, 1975	196.2	62.7	21.4	9.7	1.6

a/ Loans to the private sector; prior to 1961 data include a small amount (less than 10%) of investments other than loans.

b/ Data not available before 1970.

c/ Includes activities of the private rural bank system.

246

Table 7

GVN Budget <sup>a/</sup> 1964-75  
(VN \$ Billions)

	1964	1965	1966	1967	1968	1969	1970	1971	1972	1973	1974	1975
<b>A. Expenditures</b>												
Military	14.2	21.9	29.5	55.3	74.6	91.7	122	151	205	283	346	n.a.
Other	14.4	22.2	29.5	42.2	46.6	41.7	65	105	161	232	374	n.a.
Total	28.6	44.1	59.0	97.5	121.2	133.4	187	256	366	515	720	975 <sup>b/</sup>
<b>B. Revenues</b>												
Domestic	8.1	9.7	17.3	24.8	27.3	36.5	52	68	100	193	296	n.a.
Import	5.1	5.8	21.3	28.4	26.7	51.0	71	111	47	53	47	n.a.
Total	13.2	15.5	38.6	53.2	54.0	87.5	123	179	147	246	343	372 <sup>c/</sup>
<b>C. Deficit Before Foreign Aid (A-B)</b>												
	15.6	28.6	20.4	44.3	67.2	45.9	64	77	219	269	377	603
<b>D. Foreign Aid (Counterpart)<sup>d/</sup></b>												
	7.8	11.9	23.1	38.8	29.2	31.6	33	41	109	133	258	-
<b>E. Deficit (C-D)</b>												
	7.8	16.7	(2.7)	5.5	38.0	14.3	31	36	110	136	119	-
<b>Deficit as % of Expenditures</b>												
	28.6	37.9	(4.6)	9.3	31.4	10.7	16.6	14.1	30.1	26.4	16.5	-
<b>Dom. revs. as % of expenditures</b>												
	28.3	22.0	29.3	25.4	22.5	27.4	27.8	26.6	27.3	37.5	41.1	-

a/ Actual expenditures and revenues

b/ USAID estimate

c/ GVN/USAID estimate

d/ National Bank deposits to the Counterpart Fund rather than transfers from the Counterpart Fund to the Budget. Data equate roughly to CIP imports plus GVN uses portion of PL 480 Title I imports.

28

Table 8

GVN Official Exchange Reserves 1955-74  
(U.S. \$ Millions)

End-Year	(1) Gold	(2) Foreign Exchange	(3) SDRs	(4) Subtotal (1+2+3)	(5) IMF Gold Tranche	(6) Blocked French Francs	(7) Total (4+5+6)
1955	20	104	-	124	-	-	124
1956	20	112	-	132	-	-	132
1957	20	118	-	138	-	-	138
1958	20	139	-	159	-	-	159
1959	20	151	-	171	-	-	171
1960	20	196	-	216	-	-	216
1961	20	155	-	175	-	-	175
1962	20	133	-	153	-	-	153
1963	20	155	-	175	-	-	175
1964	20	115	-	135	6	-	141
1965	20	152	-	172	6	-	178
1966	26	275	-	301	6	-	307
1967	24	300	-	324	10	-	334
1968	24	295 <sup>a/</sup>	-	319	10	7	336
1969	24	236 <sup>a/</sup>	-	260	10	6	276
1970	24	195	7	226	16	6	248
1971	26	212	14	252	17	6	275
1972	26	207	21	254	17	7	278
1973	28	122	24	174	19	8	201
1974	30	167	24	221	19	8	248
Mar. 1975	30	127	25	182	19	8	209

a/ Includes "rice escrow account" of \$50 million in 1968 and \$42 million. These were dollar deposits in escrow at the U.S. Treasury against Vietnamese purchases of U.S. rice.

Source: IMF

248

Table 9

Simplified Balance of Payments 1964-74  
(\$ Millions)

	1964	1965	1966	1967	1968	1969	1970	1971	1972	1973	1974
<b>A. Balance of Trade</b>											
Exports	49	40	25	22	16	15	12	12	23	60	75
Imports, c.i.f. <sup>a/</sup>	-233	-288	-572	-635	-548	-689	-692	-714	-678	-717	-787
Balance of Trade	-184	-248	-547	-613	-532	-674	-680	-702	-655	-657	-712
<b>B. U.S. Support</b>											
U.S. Aid	139	203	335	347	239	265	302	340	418	438	625
(CIP)	(105)	(155)	(259)	(194)	(101)	(177)	(181)	(259)	(284)	(253)	(419)
(PL 480 Tit.I)	( 34)	( 48)	( 76)	(153)	(133)	( 88)	(121)	( 81)	(118)	(153)	(203)
(Direct Dollar Support)	( - )	( - )	( - )	( - )	( - )	( - )	( - )	( - )	( 16)	( 32)	( 3)
U.S. Piaster Purchases	15	126	333	327	301	347	318	403	213	96	97
(Official)	( 8)	( 92)	(233)	(212)	(246)	(301)	(278)	(271)	(136)	(n.a.)	(n.a.)
(Personal)	( 7)	( 34)	(100)	(115)	( 55)	( 46)	( 40)	(132)	( 77)	(n.a.)	(n.a.)
Total U.S. Support	154	329	668	674	540	612	620	743	631	534	722
<b>C. Other Donor Aid</b>	-	-	-	-	-	-	-	-	-	-	26
<b>D. Net Invisibles and Other</b>	- 11	- 41	+17	-36	+ 7	+ 5	+ 27	- 35	+ 13	+ 43	+ 9
<b>E. Change in Reserves fr. Operations (A+B+C+D)</b>	- 41	+ 40	+138	+25	+ 15	- 57	- 33	+ 6	- 11	- 80	+ 45

276

Table 9, page 2

	1964	1965	1966	1967	1968	1969	1970	1971	1972	1973	1974
<b>F. Monetary Changes:</b>											
IMF Gold Tranche +	6	-	-	-	-	-	-	-	-	-	-
Allocation of SDRs	-	-	-	-	-	-	+ 7	+ 7	+ 7	+ 3	-
Currency Revaluation	-	-	-	-	-	-	-	+ 3	+ 1	+ 5	+ 2
<b>G. Change in Reserves (EFF)</b>											
(National Bank)	- 35	+ 40	+138	+25	+ 15	- 57	- 26	+ 16	- 3	- 72	+ 47
(Commercial Banks)	(-34)	(+37)	(+129)	(+27)	(+ 2)	(-60)	(-28)	(+27)	(+ 3)	(-77)	(+47)
(Commercial Banks)	(- 1)	(+ 3)	(+ 9)	(- 2)	(+13)	(+ 3)	(+ 2)	(-11)	(- 6)	(+ 5)	( - )
<b>H. Reserves, End-Year</b>											
(National Bank)	145	185	323	348	363	306	280	296	293	221	268
(Commercial Banks)	(141)	(178)	(307)	(334)	(336)	(276)	(248)	(275)	(278)	(201)	(248)
(Commercial Banks)	( 4)	( 7)	( 16)	( 14)	( 27)	( 30)	( 32)	( 21)	( 15)	( 20)	( 20)

a/ Commercial imports only. Excludes Project and PL 480 Title II

b/ Gold, foreign exchange, SDRs, IMF Gold Tranche, and blocked French francs (see Table 8)

Sources: National Bank of Vietnam; IMF; MACV Piaster Expenditure Reports

250

Table 10

Commercial Import Payments, Nominal and Real, 1964-74

## A. Imports by Category of Financing (\$ Millions)

	CIP	PL 480 Title I	GVN	Aid Freight <sup>a/</sup>	Other Donor	Total
1964	105	34	91	3	-	233
1965	155	48	78	7	-	288
1966	259	76	221	16	-	572
1967	194	153	262	26	-	635
1968	101	138	281	28	-	548
1969	177	88	403	21	-	689
1970	181	121	360	30	-	692
1971	259	81	351	23	-	714
1972	284	118	249	27	-	678
1973	253	153	281	30	-	717
1974	419	203	196	43	26	887

<sup>a/</sup> GVN payments for freight on AID financed imports.

## B. Total Imports, Nominal and Real

	Import Payments	Import Price Index	Real Imports		
			\$ 1964	Total (1964=100) Total	Per Capita <sup>a/</sup>
1964	233	100.0	233	100	100
1965	288	102.0	282	121	118
1966	572	104.2	549	236	224
1967	635	105.2	598	257	238
1968	548	107.0	512	220	199
1969	689	110.5	624	268	236
1970	692	116.3	595	255	219
1971	714	119.9	595	255	213
1972	678	132.8	511	219	178
1973	717	179.3	400	172	137
1974	887	274.3	323	139	108

<sup>a/</sup> Assumes population growth rate of 2.6%.

251-

Table 11

PADDY (OR PADDY EQUIVALENT) AVAILABLE FOR  
ALL USES AND POPULATION INDEX, 1964-74  
(000 metric tons)

Crop Year Begin. May 1	Domestic Production Excluding Exports	Rice Exports (Paddy Equivalent <sup>1/</sup> )	Rice Imports and Stock Changes <sup>2/1/</sup> (Paddy Equivalent <sup>2/</sup> )	Paddy or Paddy Equivalent Available for all uses	Index of Paddy for Domestic use 1964 = 100	Index of Population 1964=100 <sup>3/</sup>
1964	5,200	48(80)		5,200	100.0	100.0
1965	4,800	--	130 (217)	5,017	96.5	102.6
1966	4,300	--	434 (723)	5,023	96.6	105.3
1967	4,700	--	750 (1,250)	5,950	114.4	108.0
1968	4,400	--	515 (858)	5,258	101.1	110.8
1969	5,100	--	599 (998)	6,098	117.3	113.7
1970	5,500	--	471 (785)	6,285	120.9	116.6
1971	6,100	--	234 (390)	6,490	124.8	119.6
1972	5,900	--	251 (418)	6,318	121.5	122.8
1973	6,600		383 (638)	7,238	139.2	126.0
1974	7,100		107 (178)	7,278	140.0	129.3

<sup>1/</sup> One metric ton of paddy equals 0.6 metric tons of rice

<sup>2/</sup> This column shows the combination of imports and reserve stocks employed for current year's use. Since data are not available on reserve stock changes prior to 1968, they are assumed to be constant from year to year prior to that date.

<sup>3/</sup> Assumes population growth rate of 2.6 percent p.a.

Source of production estimates: GVN Ministry of Agriculture and USAID.

25

Table 12

Exchange Rates 1955-75  
(all rates expressed in terms of piaster per dollar)

Date	Official Rate for U.S. Purchases <sup>a/</sup>	Invisibles Rate	Imports GVN	CIP	Exports	Accommo- dation Rate
1955-57	35	73.5	35 <sup>b/</sup>	35	35	73.5
1957-61	35	73.5	35 <sup>b/</sup>	40 or 42	48.48	73.5
1962-66	35	73.5	60	60	60 <sup>c/</sup>	73.5/118
Sept. 1965						118
June 18, 1966	80	118	118	118	118 <sup>d/</sup>	118
Oct. 1, 1967	118					
Oct. 5, 1970			118/275 <sup>e/</sup>		275	118
June 7, 1971			118/400 <sup>f/</sup>			
Nov. 15, 1971		410	400	275	410	410
<u>1972</u>						
Feb. 12			405	280		
Mar. 6			410			
Apr. 1	410					
Apr. 29		420			420	420
May 22					500	
June 18		425				425
July 9				290		
July 28		430		295	550 <sup>g/</sup>	430
Aug. 22		435		300		435
Oct. 30		445				445
Dec. 9		455		310		455
Dec. 30		465		320 <sup>h/</sup>		465
Jan. 3					565	
Jan. 26		475		330 <sup>h/</sup>	575	475
Mar. 7				360 <sup>h/</sup>		
Apr. 27		485		380 <sup>h/</sup>		485
May 19		500		400		500
Sept. 6		510		410		510
Oct. 2		520		420		520
Oct. 16		525		425		525
Nov. 12		535		440		535
Dec. 6		550		455		550
<u>1974</u>						
Jan. 4		560		465		560
Jan. 14				<u>1/</u>	598 <sup>1/</sup>	
Feb. 4		575			604	575
Mar. 3		590		<u>k/</u>	619	590
Mar. 25		605			635/684 <sup>1/</sup>	605

Date	Official Rate for U.S. Purchases <sup>a/</sup>	Invisibles Rate	Imports GVN	CIP	Exports	Accommo- dation Rate
<u>1974</u>						
Apr. 24		620			651/701	620
July 5		630			661/712	630
July 10		640			672/723	640
Aug. 23		655			688/740	655
Sept. 26		670			703/757	670
Dec. 10		685			753/788 <sup>m/</sup>	685
<u>1975</u>						
Jan. 21		700			770/805	700
Mar. 10		725			797/834	725

NOTE: 1) After June 18, 1966 entries made only when rates were changed.  
 2) Most PL 480 Title I imports were valued at the GVN import rate.  
 The CIP rate applied at times to imports of cotton and wheat.

- a/ Also the GVN official rate, except during the period, Oct 1, 1967 to Nov. 15, 1971 when the official rate was 80. The 80 rate, however, was applied to very few transactions during this period.
- b/ Most imports were subject to surcharges that brought the effective rate to a range of 74 to 110.
- c/ In practice, applicable only to rice. Most exports received premiums ranging from 5 to 15 piasters. The export rate for rubber was 48.65:1.
- d/ All exports except rubber which was subject to a rate of 60:1.
- e/ About one-third of GVN imports were subject to 275 rate.
- f/ The 275 "parallel" rate plus a perequation tax of 125 piasters.
- g/ Plus an additional 25 piasters for exports of products new to Viet Nam for a one year period.
- h/ PD-31 imports subject to an additional perequation tax of 75 piasters.
- i/ Exchange rate differential (between CIP and GVN imports) replaced by a rebate on CIP goods, initially set at 85 piasters.
- j/ Export premium replaced by an "interest rate subsidy" equivalent to a five percent premium.
- k/ CIP rebate changed to 60.
- l/ Interest rate subsidy changed to 13 percent for products of the fisheries, forestry, tea, and rubber industries.
- m/ Interest rate premium changed to 10 percent, except 15 percent for products of industries affected by the fuel crisis: fisheries, forestry, tea, and certain manufactured goods.

Table 1 3

BLACK MARKET AND LEGAL EXCHANGE RATES  
1965 to 1974

Year	March		June		September		December	
	Black Market Rate	Legal Rate						
1965	143	73.5	140	73.5	152	118	169	118
1966	166	118	188	118	168	118	172	118
1967	173	118	158	118	151	118	167	118
1968	166	118	178	118	203	118	200	118
1969	194	118	202	118	225	118	360	118
1970	418	118	382	118	426	118	388	275
1971	403	275	374	275	366	275	414	410
1972	445	410	417	425	424	435	495	465
1973	540	475	491	500	518	510	554	550
1974	600	605	621	620	665	670	795	685

Note - End of Period Rates: Black Market Rate-Piasters per one U.S. dollar for US\$ 10 Green.  
Legal Rate-Piasters per one U.S. dollar for personal piaster purchases.

Table 14

BLACK MARKET PREMIUM/DISCOUNT FOR \$10  
(End of Quarter Rates, 1964-74)

Percent Premiums (Discount)\*

Year	March	June	September	December
1965	95	90	29	43
1966	41	59	42	46
1967	47	34	28	42
1968	41	51	72	70
1969	64	71	91	205
1970	254	224	261	41
1971	47	36	33	1
1972	9	( 2)	(2)	6
1973	14	( 2)	4	1
1974	( 1)	( -)	(1)	16

\*Premium or (discount from) the legal exchange rate for personal piaster purchases.

RURAL DEVELOPMENT & FIELD OPERATIONS

"The Emperor's laws stop at the village gate."

- Vietnamese Proverb

At no other time in its history has the Agency for International Development, or its predecessors, employed Americans as advisors in rural areas to the extent they were used in South Viet Nam. In 1969, at the height of A.I.D.'s field effort, 1,084 direct hire U.S. advisors were assigned to field or field-management positions, more than half of the 1,846 A.I.D. direct hire employees in South Viet Nam. There were additional A.I.D. personnel resources committed to the field effort including officers on loan from other agencies as well as contract officers. This massive buildup was not a concept entirely embraced by A.I.D. but one brought about by both U.S. Congressional and Executive pressures for additional programs, tighter American controls on these programs, and greater use of American technicians as operators rather than advisors.

A.I.D. field-advised rural development operations in South Viet Nam fall into three general periods.

1. From 1954 through 1958 the United States Operations Mission in Saigon (USOM) assigned officers to provinces under the management of the Field Service Division of USOM. They were involved initially, as was most of the mission, in responding to the needs of refugees fleeing the North under provisions of the Geneva peace agreement on Indochina. These officers also worked in a limited fashion stimulating rural self-development projects under programs established by the Vietnamese government and supported by USOM funds and commodities.

2. By direction of the Executive Branch of the U.S. Government, USOM made a radical departure from normal economic assistance programs in 1962 and entered the field of civil counterinsurgency. This remained the basic mission of A.I.D. field advisors throughout the balance of the U.S. involvement in South Viet Nam.

3. A.I.D. field advisors were removed from direct control of the USAID (formerly USOM) Saigon mission in 1966 and placed first under control of a deputy ambassador and later under the U.S. Military Assistance Command in Viet Nam (MACV) in 1967.

A common goal ran through all these periods of USAID's field efforts in the country. Whether the mission was defined as development or counterinsurgency, the goal was to gain the support and loyalty of the rural population for the Government of South Vietnam. The means selected to attain this goal included improving the economic and social lot of rural Vietnamese by stimulating GVN rural programs; improving delivery of local government services by strengthening local governments; and encouraging private sector innovations which would lead to greater productivity. Behind all of these activities lay the hope that the rural Vietnamese population, perpetual target of the Viet Cong, would be less vulnerable to communist propaganda as they were drawn closer to their own government.

The terms used to describe these efforts changed frequently through the years. And as is the case with living languages, the terms, once placed under stress, developed a putty-like quality which caused them to take on different meanings during different periods. There were even differences during the same period when various U.S. and Vietnamese

groups and individuals defined their own specialized meanings for these words and phrases. Some of the more frequent terms in use during the U.S. involvement were "pacification," "counterinsurgency," "rural construction," "revolutionary development" and "civic action."

It would seem that a clear distinction might be made between "counterinsurgency," which refers to actions taken against an enemy insurgent and "pacification" which is an English approximation of an ancient Vietnamese term referring to actions taken to attract the population to the government. But these terms were often used interchangeably and after some time there was confusion in the user's mind as to whether "pacification" or "counterinsurgency" was the more comprehensive term. In later years, "pacification" was used in English more and more to connote those military activities which were being taken to gain control of a population and the term "counterinsurgency" fell into misuse. "Development" became the most frequently used term at first among civilians and it generally seemed to refer to the process of improving the services of civil government in rural areas. The terms "revolutionary development," "rural development," "rural construction" and "civic action," also referred at various periods to programs aimed at military and civil actions, or both, which brought rural Vietnamese closer to the Government of South Viet Nam. For the purpose of this narrative, the process which involved U.S. civil foreign aid field advisors will be referred to as rural development, a term which generally describes the programs with which USAID advisors were concerned, whatever the stated purpose of these programs or whatever alternate terms were used to describe the various activities.

260

### Early Attempts at Field-Advised Rural Development

Although there were no large scale efforts by insurgents to disturb GVN programs in 1954, the communists were laying a groundwork for future activity. The end of the French-Indochina War that year, left Viet Nam at relative peace, except for the activities of three armed sects (Hoa Hao, Cao Dai and Binh Xuyen) within Viet Nam which were eventually brought under control by the new government of President Ngo Dinh Diem. Under the Field Service Division of USOM, U.S. advisors coped with day-to-day province problems in receiving and settling the more than 900,000 refugees from the Hanoi regime and made proposals for development projects which seemed desirable from their vantage point. They attempted to work with President Diem's Civic Action cadre teams, which had been assigned to carry out myriad programs in rural areas, including building schools and medical facilities, repairing roads, providing water and irrigation facilities, teaching, forming self-defense groups and conducting political meetings.

### The Pitfalls of Rural Development

The political events of the time militated against a lasting U.S. success in field advisory efforts. President Diem, fearing a resurgence of guerilla activity, saw the Civic Action Cadre as a counterinsurgent force, and later, when Diem's brother Nhu, gained control of the cadre, they were looked on as a political force to bring rural people in line with a strongly centralized government. Hence, one major GVN force which might have been applied towards developing local initiative, was in fact directed into strengthening the central government.

The direction of Diem's governmental philosophy was opposite to that of the field advisory effort. He worked to build a strong central

government which could control the country. He abolished village elections and replaced elected village officials with appointed ones who would respond to demands from the province government, which was in reality an extension of the central government. On the other hand, the message conveyed by USOM's field effort, sometimes implied, sometimes expressed, was the need for stronger, more decentralized local governments which could act with some independence in solving their local problems. Diem was suspicious of Americans in rural areas. And when confronted with a specific proposal from USOM that province representatives be utilized to assist the province chiefs with direct programs of aid, he rejected the idea on grounds that the province chiefs were too busy.

Within USOM, there was also a somewhat circumspect attitude with respect to a field advisory effort. The various technical divisions dealing with programs such as agriculture, education and public health, were less than enthused over the role of province field advisors. They were concerned with their own programs, as promulgated through the central ministries and did not wish to become involved with field advisors independently controlled by the Field Service Division. Lacking any mission of substance, the Field Service Division was disbanded in 1958.

During the absence of U.S. field advisors from 1959 through 1961, the Vietnamese government continued with experiments at controlling the population and separating it from the Viet Cong. There was the inescapable requirement to address social and economic problems. And such programs were at least planned by GVN even though their success was limited at best. After experimenting with an attempt to group Viet Cong sympathizers and supporters of the Saigon government into separate

living areas in February, 1959, the GVN moved to another approach in April--agrovilles. Unlike its predecessor, the agrovillage program was primarily an attempt to build social and economic centers. This program too was abandoned in 1961. Although the agrovillage approach failed because of disapproval of the residents who had been moved into them, its successor, the satellite agro-hamlets program, was judged more favorably by GVN. In these smaller hamlets, people were not so far removed from their lands. It is at this point that the Vietnamese government made, what in the light of later events, proved to be a costly mistake: It selected the hamlet level of government as the level to receive the government's attention, thereby shunting aside the more viable, larger village level of government. As the proverb quoted at the beginning of this section indicates, the Vietnamese rural people held their village governments in great regard as a protector against overly repressive actions by the central government.

For better or worse, the dye was cast and the agro-hamlet program was developed into an even more ambitious approach to civil defense which would be known as the Strategic Hamlet (Ap Chien Luc) program in 1961.

#### The Establishment of the Viet Cong

When the Viet Minh cadres withdrew from South Viet Nam in 1954, they took a number of steps which strongly suggested they would be back. First they told Vietnamese who stayed behind in the villages that they would return and punish those who collaborated with anti-Viet Minh forces. They buried caches of arms. They left agents behind. Many of them did return during the ensuing years, to recruit, to organize and to begin operations against their enemy, the Republic of Viet Nam.

The agents left behind and those who returned later after training in the North, became known as the Viet Cong (VC) a contraction of the phrase "Viet Nam Cong Sang," translated "Vietnamese Communists." They were renamed by Southerners in order to distinguish them from the Viet Minh movement, which was considered more nationalistic in nature. The Viet Cong were so designated to show the changes which had taken place within the Viet Minh movement after Ho Chi Minh, a declared communist, established himself as head of the North Vietnamese government. The Viet Cong described themselves in a more nationalistic tone, "The National Liberation Front" (NLF). By 1954, the Viet Cong were building an organization which could expand isolated acts of terrorism into a full blown insurgency.

Their target was rural Viet Nam, unlike the communism of the west where urban areas more often than not were the main objectives. Their methods were copied from the successful Chinese Communist Party which had overthrown the government of Chiang Kai Shek in 1949. A major objective of the North Vietnamese during the immediate post independence period was to develop Gen. Vo Nguyen Giap's "People's Army" in the South. Their tactics appeared to have precluded the need either of weapons heavier than mortars or large numbers of soldiers, fighting only when they momentarily held numerical superiority in a given battle, and running to fight another day or night when outnumbered. They fought primarily at night. They had no permanent installations to guard, such as camps, towns, roads or bridges. In fact, they operated best where there were no driveable roads and bridges. Where they were successful they forced their enemies either to dismount and attempt to

264

find them on foot or give up the chase.

The Viet Cong judiciously balanced selective terrorism against such bait as land reform programs, status in the community, and promises of ever greater rewards to come when final victory was achieved. Their frequent night visits to hamlets which they did not control in the daytime left behind a clear message to the rural Vietnamese. If the villagers cooperated with the GVN they would be punished, perhaps killed. On the other hand if they supported the Viet Cong covertly or openly, as the situation permitted, they would be rewarded.

GVN efforts at pacification up to 1961 had been received at best as mixed blessings by the rural Vietnamese. Attempts to force Vietnamese into secure hamlets or villages, had created many resentments among the Vietnamese people. Failures of local governments to live up to central government promises had generated further dislike towards the government. Abuse at the hands of soldiers and government officials had added still another group of at least passively dissident people to the rural areas. The Viet Cong capitalized on local dissatisfactions, giving an alternative organization to which rural people could bring their grievances. They spent a great deal of effort identifying unpopular local officials and repressive local military forces. When executing a local official, they often gathered residents together to witness the execution. After reading a list of grievances against the official and executing him, they would leave the bill of grievances attached to his body.

The Viet Cong needed support or at least neutralism on the part of rural people in order to survive. They also needed rice to eat, money for supplies and intelligence about their enemy. So the Viet Cong

265

pursued the cultivation of rural people by the balanced use of terrorism and reward.

All GVN attempts at pacification or rural development presented a threat to the Viet Cong. To thwart government progress the VC would target on development projects, even destroying medical facilities and schools at times, always careful to explain to the local populace why they were forced to take such actions. Because they chose their targets selectively, they were often able to provide creditable arguments for their actions. Destruction of educational facilities was accompanied by arguments that the projects were funded by "American imperialists" or that the existence of the project signified that the villagers were collaborating with the GVN. Bridges and roads were destroyed on grounds that they had been built, not to serve the villagers, but to provide easy access to the areas for government soldiers.

Viet Cong activities created such concern by late 1959, that the U.S. Army Chief of Staff, General Lyman L. Lemnitzer visited South Viet Nam for an assessment. He concluded that the situation had deteriorated markedly. A request for increased U.S. assistance by President Diem was supported by Lemnitzer, who recommended that the training and organization of the Vietnamese Army should be shifted in emphasis from conventional to anti-guerrilla warfare training. In the following months, U.S. military advisors assigned to field advisory duties at battalion levels were increased. In 1960 the Civil Guard and Self Defense Corps were transferred from the Ministry of Interior to the Ministry of Defense for training. U. S. Special Forces / <sup>trained the new</sup> 5,000-man Vietnamese Ranger Force. During the next few years, U.S. military advisors were stationed at province and district levels to advise Vietnamese province chiefs on use

266

of local security forces against the insurgents.

During the late 1960's, the Vietnamese government promoted heavily the theme, "The Government rebuilds; the Viet Cong destroy." It was an apt description of the physical movement of the war. To complicate the position of the government, each building or road or bridge that it built required an additional input of security forces to prevent the Viet Cong from destroying the facility again. Viet Cong regular forces had reached an estimated strength of 24,000 by 1963 with perhaps two to three times that number of irregulars. By 1965, the regular forces were estimated at 73,000 with a corresponding increase in irregulars. Their ability to fight only on their own terms then seemingly disappear when sought, left the Vietnamese defense forces frustrated. By 1963, the Viet Cong were killing more than 2,000 civilians a year. They were kidnapping more than 7,000, many of whom were later released after attempts were made to reorient their thinking. Many rural Vietnamese lived in terror of the sound of footsteps in the night. Vietnamese military forces had found no way to protect people from this effective form of Viet Cong conditioning.

Not only were the military forces baffled over protection of rural areas, the highly centralized government ministries were equally unable to provide adequate government services in rural areas.

#### The Reestablishment of the USOM Field Effort

It was amid these circumstances that USOM advisors found themselves tasked, in 1962, with the job of producing a civil counterinsurgency program, heavily staffed by U.S. advisors in rural areas, which unlike the 1954-58 period, were peppered with large-scaled violence. The

decision to reinstate a field advisory effort and redirect USOM's interests from development to counterinsurgency grew out of a U.S. reassessment of the growing insurgency, which had become a serious threat against the survival of the Government of Viet Nam. Concluding that direct, short-term actions must be taken to ensure that survival, President Kennedy agreed to press for more military and civil aid for South Viet Nam. Assessments of the situation in Viet Nam brought back to Washington by Gen. Maxwell Taylor and others in 1961, convinced the Kennedy Administration that both civil and military redirection of U.S. efforts were necessary if the Republic of Viet Nam were to survive. Opinion was divided within A.I.D. as to the propriety of the Agency dealing with short-term counterinsurgency programs. Those who opposed the Agency's involvement argued that A.I.D.'s best contribution to South Viet Nam's stability would be the continuation of programs designed to strengthen Vietnamese institutions and thereby produce orderly economic and social development. They felt that the guerrilla crisis could best be handled by the military. Those who argued in favor of counterinsurgency activities believed that, given the realities of the situation there simply was no alternative, i.e., if the immediate threat to survival was not met, there would be no longer term tomorrow to develop for. This conflict over the two possible courses of action became acute in 1962-63 and continued for some years after.

President Diem, who had refused permission for advisors to work with province governments in 1958, had not changed his mind. He rejected a USOM proposal for this second deployment of USOM officers in the provinces. Despite the President's reservations, USOM sent some officers

to the field informally for several months. Pleased with their utility to the overall U.S. Mission, the effort was expanded to other provinces with the knowledge and occasional collaboration of President Diem's brother, Nhu. Within two years, provincial representatives were stationed in most provinces of Viet Nam. This field operation was originally named the Office of Rural Affairs but later was changed to the Office of Field Operations.

In its initial stance, USOM's second field effort in 1962 consisted not of technicians but generalists who were stationed at the province level. They were tasked with expediting implementation of rural programs. They also offered support to the Strategic Hamlet Program which had been instigated by the GVN the preceding year. The frictions which had been created between field advisors and USOM technicians in Saigon during the 1954-58 period returned to USOM again in 1962, with the establishment of the new office. The field effort provided the Mission Director with a new line of authority to the province which cut across the technical divisions' established lines of control. However, the major portion of USOM's project funds continued to be dispensed through the technical divisions. Meanwhile, there was growing disenchantment among Americans in the field with the ability of Vietnamese ministries to deliver services in rural areas which would fulfill the concept of short-term, high impact programs designed to lure the Vietnamese people closer to their government.

If the Americans found themselves with organizational problems, theirs did not compare with the unwieldy Vietnamese structure nor with the jealousies and frictions within which it had to operate. The central

269

ministries remained somewhat aloof from executive control, conducting their affairs in such areas as education, agriculture, public works and public health without any strong response to the desires of the Chief Executive. At the province level, the province chief who was more responsive to the President's desires, found the same resistance to executive authority in dealing with province technical services. Civil servants who staffed these offices were hired, paid, promoted and fired by the Saigon ministries and were more apt to respond to authority from that direction rather than from the office of the province chief, who was normally a military officer.

Support of the Strategic Hamlet Program proved to be a frustrating and disappointing experience for USOM and its province representatives. The stated Vietnamese goals were to:

- Make a census of and eliminate Viet Cong infrastructure within the hamlet.
- Organize a civil defense system.
- Complete physical defenses.
- Organize secret cells.
- Conduct hamlet elections by secret ballot.

The Vietnamese government counted 12,000 hamlets in South Viet Nam during this period. By September 1962, the government reported that 3,235 hamlets had met the goals of the Strategic Hamlet Program. By November 1963, GVN increased that figure to 8,544. But some months prior to that, USOM's field staff in the Delta provinces cautioned the Mission that the program was neither being thoroughly executed nor properly reported.

Attention to pacification programs was abruptly interrupted by the overthrow of the Diem government and the killing of Diem and his brother, Nhu on November 2, 1963. The central government was paralyzed by the inability of any one man or group to re-establish authority in Saigon. The Viet Cong rushed into rural areas, seizing large sections of the countryside and local governments were forced to retreat from hamlets and villages to the district and province towns. Whatever progress the government had made towards controlling or even staying in touch with rural people disintegrated.

Reassessments of the Strategic Hamlet Program in May 1964 suggested that only about 6,500 hamlets met the program criteria. By December 1965, the number of satisfactory hamlets was listed at 3,800 out of the country's 12,000. The Strategic Hamlet Program was, for all intents and purposes, finished.

Although efforts were made at pacification by lower levels of government during 1964, the national program remained dormant while chaos reigned in the Executive Office. One government after another rose and fell. Much of 1964 was spent by those involved in the rural development effort in attempting to plan a rural program alternative to the disastrous Strategic Hamlet Program.

Whereas 1964 proved disappointing to Americans and their Vietnamese allies, the events of 1965 brought some encouragement. The first U.S. tactical troops, vanguard of an eventual force of 540,000, landed at Da Nang and the total number of U.S. tactical forces reached 170,000 by the end of the year. In July, Henry Cabot Lodge was reappointed Ambassador to South Viet Nam as Air Marshall Nguyen Cao Ky was stepping

into the role of Vietnamese premier, the first contender since Diem to bring a degree of stability to the President's office.

A principal missing key in rural development was a Vietnamese agency capable of formulating and managing rural programs. By this point, hopes of utilizing the government's staid ministries had faded, and both U.S. and Vietnamese sought some method of by-passing the traditional constraints of central ministries. The existing pacification element in the Vietnamese government was known as the Rural Reconstruction Council. Premier Ky quickly elevated the council to ministry status. The name was eventually changed in Vietnamese to the Ministry of Rural Development (MORD). (For some reason Americans adopted the translation "Ministry of Revolutionary Development." As a linguistic accommodation, the Vietnamese referred in English thereafter to the organization as the Ministry of Revolutionary Development. Some years later, the Americans readjusted their terminology to the original Vietnamese meaning.)

The Vietnamese and their American counterparts were picking up the pieces in their shattered pacification program. Unfortunately, the first minister of MORD, Mr. Nguyen Tat Ung, was killed in an air crash 60 days after his appointment. To replace him, Premier Ky selected the aggressive Maj. Gen. Ngyen Duc Thang, who pressed the cause of rural development with a zeal that impressed the Americans who saw him in action.

MORD was dubbed a "super-ministry" by friends and foes alike. There was the predictable dissatisfaction among the line ministries which saw MORD as a threat to their jurisdictions. And there were others who perceived MORD as capable of being a super ministry in every sense of the word. It possessed a streamlined fiscal system which allowed it to dispense funds quickly without red tape. It was given authority to provide hamlets with almost any government service which might be desired within the limited perception of the Vietnamese peasant. It had the full backing of the Premier and of the U.S. Government. MORD inherited an embryo pacification program which had been in planning for more than 1 year and was given a 1966 program budget of 2 billion piasters.

These funds were provided from USAID generated piasters and were allocated by MORD to the provinces for the following uses:

Programs	Funds allocated (VN)	Percentage
Settlement	264,125,000.	16.92
Rural Development cadre	38,994,000.	2.50
Development of self-sufficient hamlets (Self-help program)	138,550,000.	8.87
Rural education	295,470,000.	18.92
Hydraulics	76,477,000.	4.90
Agriculture and animal husbandry in the Highlands	59,725,000.	3.82
Cattle	56,251,000.	3.60
Pisciculture	46,394,000.	2.98
Bridges and roads	330,563,000.	21.17
"Open arms" operation	104,747,000.	6.70
Earth work (foundations for refugee housing)	9,579,000.	0.62
Transportation	68,144,000.	4.37
Warehouses	26,184,000.	1.68
Unexpected expenses	<u>46,000,000.</u>	<u>2.95</u>
TOTAL:	1,561,208,000.	100.00

The balance of MORD's 2 billion piaster budget was reserved for additional allocations to provinces which executed their initial programs with dispatch.

The MORD rural programs which had been developed by 1966 were diverse and included heavy dependence on the establishment of military security. The GVN considered that 3,620 of the country's 10,000 to 12,000 hamlets were suitably pacified under recent programs and the commitment to continue developing them was included in the 1966 plan. The population of these pacified hamlets totalled 7,842,000, or 61 percent of the nation's population. In addition, the plan called for pacification activities in more than 2,000 additional hamlets, representing another 2 million people, or 15 percent of the population.

In terms of projects to be completed in pacified hamlets or those under pacification, the plan set these goals:

- o Resettle 41,000 families which had left Viet Cong areas.
- o Complete 2,779 hamlet self-help projects.
- o Construct 2,251 elementary hamlet classrooms and recruit 2,604 teachers for hamlet schools.
- o Construct 913 kilometers of roads, and 19 larger bridges, ferries and markets and 129 smaller facilities.
- o Construct 14 large dams and dikes and 43 smaller ones.
- o Restore or build 119 kilometers of canals.
- o Train 3,700 farmers in improved agricultural techniques, issue seeds, distribute 61,000 chickens and ducks and 16,000 pigs to promote the livestock industry.

o Construct 20 rural electrification projects.

A unique feature of MORD was its personnel structure. The vast majority of its employees was assigned to the hamlet level. At its zenith, 1969, MORD had at its disposal more than 40,000 Rural Development cadres, most of whom worked in hamlets. The cadre teams were tasked with serving as substitute hamlet governments where they were assigned. After a period of organizing the hamlet, during which school classrooms, health stations or other facilities were built under their guidance, they were expected to supervise the election of hamlet chiefs, then move on to the next assigned hamlet and repeat the process. Performance was spotty, but the program appeared less like a pre-ordained disaster than its predecessors and more like the beginning of a viable rural program.

This new ministry had its share of problems as well. The cadre was created from several other cadre organizations which had been in existence prior to that time but additional recruits were generally untrained and poorly inspired. They were dressed in black pajamas and armed. In order to survive, they had been organized into 59-man teams, with most members serving as security forces in the insecure countryside. The Office of the Special Assistant to the U.S. Ambassador (OSA) had responsibility for training the Rural Development cadre while USOM provided technical support and counterpart funds. Each cadreman received ten weeks training, which was provided as rapidly as facilities at the Vung Tau National Cadre Training Center would permit.

The Ministry also had the problem of national arithmetic which plagued its predecessors: 12,000 hamlets and only limited resources to cope with them.

275

But within these constraints, the organization set about its work.

The cadre teams were immediately targeted by the Viet Cong. The military security promised by the Vietnamese Army and province chiefs frequently did not appear, or if it did, it retreated to more secure areas before the night was far gone, leaving the cadres to fend for themselves. Because of this insecure situation, the cadres themselves often left their assigned hamlets at night for more secure places. The Viet Cong set about to demoralize the cadre, destroying the structures they had built and intimidating the hamlet residents from cooperating with the cadres.

It was also planned that each pacified hamlet would organize and maintain a Popular Force unit to prevent the enemy from re-entering after pacification. But in reality, there were insufficient resources to provide for a sufficient number of local units. Hence, lacking the basic prerequisite of security, pacification progress remained a tenuous thing.

USOM's field advisors, known as provincial representatives by this time, provided general advice and assistance to province governments in all civil affairs. The special interest of the province representatives was the pacification or rural development plan as it evolved in the 1960's. Many province chiefs felt inadequate in dealing with civilian technical services. In some provinces, this proved a frustrating bar towards progress since without the province chief's backing nothing could be done. In others, province representatives were able to encourage the province chief to take control and administer the services. By 1966 many provinces were staffed with one or more U.S. generalists and several specialists: An agricultural advisor, a community develop-

ment advisor and a public safety advisor. In addition, the United States Information Agency, which operated the Joint United States Public Affairs Office (JUSPAO) in Viet Nam, had fielded information advisors in many provinces.

A.I.D. inherited an unusual program in 1963: The Chieu Hoi Program. "Chieu Hoi," which translates as "Open Arms" in English, was set in motion to encourage Viet Cong to defect and rejoin the GVN and their families who had remained loyal to the established government. In the first three years of the program only 27,000 Viet Cong political and military personnel had rejoined the GVN. Early in 1966, the Vietnamese government agreed to give more priority to the program. USAID provided support in the form of camp care, training, and housing. The number of returnees rose to more than 20,000 each year during 1966 and 1967. Hoi Chanh (the returning VC) were given 45-days indoctrination and then allowed to return to their homes with a six-month draft deferment. The rate dropped in 1968, after the Viet Cong Tet offensive, then exceeded past records in 1969.

Much of the province representative's day-to-day effort was directed at pressing for development in the target hamlets of the rural development program, of assessing the work of the rural development cadremen working in these hamlets, of improving agricultural practices through the province agricultural service, of assisting with the reception and care of refugees and of assuring a proper flow of counterinsurgency commodities into province warehouse constructed with USAID assistance. These commodities consisted of cement, steel reinforcing bars, metal and mineral fiber roofing, and surplus U.S. food from the

- 211 -

PL 480 program. Additional effort was directed at programs in public health and education. The popular theme of the time was "winning the hearts and minds" of the Vietnamese people, a goal which proved far more elusive than had ever been anticipated.

By the end of 1966, less enchanted assessments were beginning to be made by Vietnamese and Americans. Despite an aura of industriousness within the Ministry of Rural Development, largely brought about by the boundless energy of its minister, it was difficult to be sanguine about the program's accomplishments in relation to the problems faced. The Minister, General Thang, concluded that MORD had spread itself too thin in too many hamlets. There were others that argued that to reduce the number of hamlets under pacification would be to slow the pacification effort to a crawl. There were compelling arguments on both sides and this dilemma, which had plagued Viet Nam for years, still stood in the way of a workable program.

Gen. Thang, unfurling the motto "Go slowly but surely," insisted that the number of hamlets to be pacified in 1967 be reduced and that more funds be concentrated in the selected ones. Although this was done, it is doubtful that anyone could have measured any difference in the results between the pacified hamlets of 1966 and those of 1967. As the GVN moved security forces into the new hamlets, they were forced to move security out of hamlets already pacified. And the Viet Cong, always waiting in the Nipa palm, were quick to move in and resume control wherever they could.

The Viet Cong had a distinct advantage here. The very nature of the war and their concept of operations allowed them to disrupt large

areas without actually holding them. They needed fewer troops to carry out their tactics of hamlet disruption. The GVN, in order to keep the Viet Cong out some of the time, had to guard the hamlet all of the time. But the Viet Cong needed only to make occasional appearances in a hamlet in order to carry out its goals of collecting taxes, propagandizing, punishing collaborators, and threatening to punish other hamlet residents if they supported the GVN. A small mobile VC guerrilla unit could disrupt several hamlets each night while the GVN had to assign a small force to each hamlet on a full-time basis in order to protect it.

#### Consolidation of U.S. Field Advisors

While the Vietnamese were attempting to address their organizational problems, the overall U.S. mission under the Ambassador was rearranging its priorities and organization to coordinate better its field operations.

American military forces in Viet Nam exceeded 400,000 by 1967 and the entire complexion of the U.S. effort, both civil and military, was altered by this influx. During the first half of 1966 a number of management problems were identified concerning the working relationships among American advisors at the province level.

Stanley Andrews, a consultant for A.I.D., described at least part of the problem in a report to Mission Director Charles Mann, based on Andrew's field trip during October 1966. "At the provincial level, one Provincial Chief after another complained not only about the Americans running out to sell some program but the pressures from his own government services." There were indeed a number of U.S. agencies represented at the province level including A.I.D. through its field

operations staff and the Military Assistance Command which had large advisory forces at the province and the district level. All of these forces were generally interested in either rural development, rural security or both.

As early as 1964, General William C. Westmoreland, who was to become the commanding general of MACV in June visited Malaysia, in the company of other key U.S. officials from Saigon and with Sir Robert Thompson, head of the British advisory team to Viet Nam. One purpose of this visit was to assess command arrangements which had been used by the British during the war in Malaya. From this trip, General Westmoreland concluded that unity of advisory command at the province level was an essential ingredient of organization.

Although civil and military U.S. province advisors had been working closely together, they had not developed a dialogue sufficient to assure a well-defined U.S. position on coordination of military and civil activities. The two vested interests, one in which civil affairs were paramount, the other in which military affairs were paramount, continually fail<sup>ed</sup> to provide a well-balanced coordination. The intensity of the war at this point demanded that civil-military priorities be meshed. It was evident that successful civil programs could not be initiated until an area was brought under and kept under sufficient military control, and this was not being done. There were even deeper problems. Central among them was the fact that there were insufficient local military forces to conduct a pacification program of any size. On the American side, this problem, as well as others related to it, had to await a resolution of the U.S. command problem before being adequately defined and addressed.

280

In early 1966, Ambassador Henry Cabot Lodge appointed Deputy Ambassador William J. Porter as coordinator of U.S. support of rural activities and charged him to reconcile roles and duties within the U.S. Mission. Ambassador Porter established a joint U.S. Agency Planning Group under his direction to coordinate planning for rural development among U.S. agencies and to participate in planning with the Ministry of Rural Development (MORD). The joint U.S./GVN efforts produced guidelines for programs and selected national priority areas for 1967. Detailed guidelines for provinces were published by the GVN on October 8, 1966. During this period, Ambassador Porter attempted to coordinate the U.S. civil effort through staff actions. But this seemed inadequate and, as a first step toward field consolidation, the decision to merge the U.S. civil advisory functions in field operations was made. In November 1966, Ambassador Lodge consolidated all U.S. civil field advisors, e.g., USAID, USIS, and OSA at the province and regional levels into single units with a single American in charge. This organization was designated the Office of Civil Operations (OCO), and the senior official at province level was more often than not the USAID province representative. Wade Latham of USAID became the first director of OCO and reported to Ambassador Porter. In principle, at least, this left the province chief with only two major U.S. personalities to deal with: The MACV sector advisor, who supervised U.S. military support in the province, and the OCO representative, who supervised civil activity.

In May 1967, Ambassador Lodge placed all field personnel in the pacification program at province, regional and national levels under MACV. This organization was designated Civil Operations,

Revolutionary Development Support (CORDS). Under this arrangement, these province teams, headed by senior military or civilian U. S. officials referred to as Province Senior Advisors, reported through their regional headquarters to the newly created post of Deputy Ambassador for CORDS, who in turn reported to the Commanding General of MACV.

One effect of these changes was to remove from the civil agencies in Saigon any direct control over their respective field advisors. It provided the single managership which was sought and placed it under MACV on the grounds that security was the prime prerequisite for pacification and rural development and that the bulk of U.S. advisory and logistic resources was already under the Military Assistance Command. Announcing the formation of CORDS, Ambassador Ellsworth Bunker, who had replaced Ambassador Lodge, described the new organization as "a unified civil military US advisory effort in the vital field of Revolutionary Development, (which) is in my view neither civil nor military but a unique merging of both to meet a unique wartime need."

The civil and military leadership of CORDS was sandwiched so that, as a general rule, a civilian found himself managing military personnel and found himself, in turn, being managed by a military officer. At the province level, military Province Senior Advisors had civilian deputies, and civilian Province Senior Advisors had military deputies. This sandwich arrangement was utilized from the district level of the country through the province and regional levels up to the top of the U.S. Mission, where the Deputy for CORDS was a civilian with ambassadorial rank, reporting to the military Commander of MACV, who in turn reported to the Ambassador. Under this arrangement, the senior advisor at each level

02

was equally responsible for civil and military programs. Such massive organizational changes obviously impacted heavily not only on the American agencies represented in Saigon but on the Vietnamese government as well.

During the transition from individual U.S. agency field staffs in 1966 to that of a single U.S. field staff in 1967, USAID began a buildup of its officers assigned to the field in hopes of placing representation in the district as well as the province and regional levels. In addition to supplying manpower for the unified field concept, USAID provided funds both for rural development programs and for administrative support of its field officers.

In a typical province team, one would expect to find a senior USAID representative who served either as the Deputy Province Senior Advisor (DPSA) or the Province Senior Advisor (PSA). The senior military officer, lieutenant colonel or colonel, filled the other position. There were one or more USAID Public Safety advisors on the staff, an agricultural advisor, one or more generalists, sometimes a social welfare or refugee advisor, all furnished by USAID. The U.S. Information Agency provided an information specialist for the staff. The Army normally provided an engineer advisor. The chief business of the province teams in 1967 was to address the prosecution of the counter insurgency program for rural Viet Nam. Additional technical assistance was available at the regional level where larger, similarly sandwiched organizations had been established to serve as links and conduits between Saigon and the field.

283-

The size of the USAID staff in Viet Nam grew, partly to provide a sufficient field staff for the expanding operations in rural areas, including the stationing of USAID officers at the district level. In May 1966, the total USAID Viet Nam staff consisted of 760 direct hire employees, 130 Americans on contract, 255 Third Country employees (mostly Filipinos), and 1,600 Vietnamese employees. By June 30, 1967, as the CORDS organization was inaugurated, there were 674 direct hire USAID employees, 219 Americans on loan from other agencies, 264 contract personnel, and more than 2,500 third country nationals and Vietnamese employees. At the end of the first year of operation, June 30, 1968 CORDS controlled 1,076 or more than 50% of USAID's total force in Viet Nam of 1977 direct hire U.S. employees. (See Attachment 1.)

#### The 1968 Viet Cong Offensive

As the Vietnamese and American governments were revamping their own organizations to deal with the burgeoning insurgency, the Viet Cong were readying their plans for massive assaults on Vietnamese provincial capitals. By October 1967, reports of heavy enemy shipments of war materials increased. The philosophy of the Viet Cong, patterned after Chinese Communist guerilla strategy, had up to this time concentrated on attempts to control the rural areas rather than the cities. But the cities provided logical targets for their attacks and the tactics increasingly included frequent harrasing attacks on more vulnerable district and province capitals, as well as Saigon itself, taking advantage of the natural animosities between rural and urban populations.

224

But the magnitude and the duration of the Viet Cong Mau Thanh offensive, launched at the beginning of the Vietnamese New Year on January 31, 1968, came as a tragic surprise to the GVN.

Both the GVN and the Viet Cong had announced cease-fires for the Tet holidays. A similar arrangement the year before resulted in a relatively peaceful holiday for the Vietnamese and in 1968, many Vietnamese soldiers had been granted leave for the holidays. More than 30 of the 44 province capitals came under attack simultaneously. Saigon was invaded by Viet Cong units and street fighting was the order of the day. Most rural development activity was suspended as U.S. field personnel found themselves under mortar and rocket attack and frequently under ground attack as well. A number of USAID field advisors were killed or wounded in the several weeks that followed. The initial attack, which was generally contained within three weeks, was followed by a second, less effective Viet Cong offensive in May. Viet Cong propaganda was aimed at driving Vietnamese out of the cities, of attempting to overthrow local governments or at least to paralyze them as well as private activity. However, in most areas of the country, normal rural development activity was resumed in two or three months. U.S. regional provincial and district teams were called on heavily to deal with the nearly one million refugees generated by the offensive. In addition to the great psychological disruption created by the VC, 12,696 Vietnamese civilians were killed, 20,000 wounded and property damages ran to the piaster equivalent of \$173 million.

-285-

The Rise of the Central Pacification and Development Council

In February, the Vietnamese Government took a step which was to influence profoundly the implementation of rural development efforts for the next seven years. The new president, Nguyen Van Thieu who had replaced Premier Ky in October 1967, formed a Central Recovery Committee to coordinate and expedite recovery efforts including the care of refugees, restoration of cities, reopening of major lines of communication and the development of a national spirit of unity.

The committee included all government ministries and was established at the highest level with the President in the chair. But in fact, working meetings were not held at this level. Lieutenant General Cao Nao Hon, the chief operative for the committee, chaired meetings which were attended, not by ministers but by representatives of each ministry. Nevertheless, the committee served well as an emergency coordinating vehicle in the eyes of GVN and U.S. officials and it was the genesis of the subsequent Central Pacification and Development Council (CPDC) which was operated from the Office of the Prime Minister. This was accomplished not without challenge from the Ministry of Rural Development which until that time had been the leading managerial force in rural activities. But the CPDC won, with American backing, and succeeded MORD as the central organization for the conduct of pacification programs.

The line ministries of the GVN, never happy with MORD's activities in their areas of discipline, had no cause to rejoice over the formation of the CPDC. MORD, although called a "super ministry", was headed by an official who had the same rank as any other minister. Hence, if the

Minister of Rural Development had any additional leverage, it was because of personal relationships with the President or the Prime minister or because of keen U.S. interest in MORD. On the other hand, the Central Pacification and Development Council not only possessed the powers formerly held by MORD in civil matters, but was influential as well in directing local military affairs. Although directed by Lt. Gen. Hon, who did not hold ministerial rank, the council's power derived from the Prime Minister, who was a supporter of General Hon, and by the President himself. The General did not hesitate to use his influence with the Prime Minister.

The Prime Minister and the President, had always found ministries unresponsive to the executive offices - they tended to operate almost as separate entities rather than part of the executive branch of government. But CPDC activities and the necessity to produce specific plans for rural areas provided the means by which the Prime Minister could gain greater control over the line ministries and the crisis created by the 1968 Viet Cong offensive, provided the opportunity to do so. In the ensuing several years, the ability of the Prime Minister to direct the ministries grew through the CPDC mechanism and its requirements for ministries to participate in rural planning.

The evolutionary nature of the U.S./GVN approach to pacification and development can be seen in these events: the U.S. moved first in 1967 to consolidate its civil and military advisors. And the following year, the emergence of the CPDC, with equal powers to direct military as well as civilian programs in rural areas, provided GVN with the beginning of consolidated management. Even

though the CPDC had offices at the province level (carved partly out of the assets of MORD) it did not have as neat a line of province management as its American counterparts had constructed through CORDS.

The Ministry of Rural Development, failing to retain its prime position in pacification, had to be satisfied with the administration of the hamlet programs.

From the standpoint of the American advisory effort, the CPDC represented at the national level, a suitable counterpart for CORDS interests, which were roughly parallel to those of the CPDC.

Although rural development programs were continued despite the offensive during 1968, perhaps the greatest contribution to the total effort by rural development advisors was made in the area of containing emergencies such as refugee generations and assisting the Vietnamese government in reestablishing lines of communication and rebuilding key government installations.

#### Mobilization of the Vietnamese Population

Although the military forces of South Viet Nam had increased from 242,000 in 1956 to 615,000 in 1967, the government had not ordered total mobilization of the populace but the traumatic effect of the 1968 Viet Cong offensive precipitated this action. In addition, the government took decisive steps to organize a functional Peoples Self Defense Force. Mobilization increased Vietnamese regular and local military forces by 100,000 troops a year through 1971, when the total military force settled at about 1.1 million men.

208

There were some side effects of total mobilization which favorably influenced the pacification program. The Vietnamese are not traditionally a mobile people. They are content to remain in their villages, many of them never venturing either to the province capital or Saigon. They resist movement and when placed under pressure to move, look for alternatives to leaving their homes. The structure of Vietnamese military forces was complex. There was the regular Army of the Republic of Viet Nam (ARVN) to which draftees were sent. This represented the least desirable choice to Vietnamese because it took them farthest from home. A second organized force, the Regional Forces (RF), were generally employed within the boundaries of the home province, and therefore presented a preferable type of military service for the home-loving Vietnamese. Then, there were the Popular Forces (PF) which were deployed in the village, or at most in the district where they were recruited. This presented the most desirable form of military service. On the debit side, from the standpoint of the draft-age Vietnamese man, the pay, the uniforms and the armament as well as general logistic support were poorer in the RF and poorer still in the PF than in the ARVN. On balance, however, enlistment in the RF and PF were favored over conscription into an ARVN unit. As a result, as the GVN and U.S. agreed to increase the Regional and Popular force units which were called the territorial security forces, their numbers swelled accordingly and local recruitment problems were solved. These territorial security forces were to become the backbone of the pacification effort, providing close-in security for the rural areas.

Mobilization also provided incentives for Vietnamese to join the

281

Rural Development Cadre, which had suffered from manpower shortages since its inception, as an alternative to being drafted into ARVN. The number of cadre units began to grow accordingly until it surpassed 48,000 by 1970.

In addition, another local security organization, (PSDF), consisting of local volunteers with the mission of protecting their hamlets and villages against the insurgents, was perfected in 1968. Although never developed to any degree of military sophistication, the PSDF did prove to be a deterrent to Viet Cong tax collectors, recruiters and propagandists. While these unpaid farmers had been the subject of organizational attempts before, only in 1968 did they receive weapons in quantity and the necessary command interest of the province chiefs to make them operational. They died in greater numbers than their Viet Cong attackers and they lost more weapons than they captured. But in spite of their record in purely combat terms, they were there and when they chose to fight, they were a force which could not be ignored by the Viet Cong. The sum of mobilization, then, was to increase the number of Vietnamese available for security as well as civil operations in the pacification programs. The increase in pacification forces in 1968 provided another partial solution to the historic problem of finding sufficient resources to pacify rural Viet Nam. Yet, the unsolved problem remained that of producing a concept to apply the growing pacification forces in a manner which would meet pacification objectives over a wide geographical area.

#### The Accelerated Pacification Campaign

Whereas the first part of 1968 was spent in recoiling from the trauma of accelerated urban war launched by the Viet Cong, the last several months

210

of the year represented a significant turning point for the GVN and for Americans participating in the rural pacification program.

In October, CORDS and the Central Pacification and Development Council, produced a plan to counter the malaise which had developed after the Tet offensive and get rural security and development programs moving again. Peace talks had begun in Paris but the war itself continued unabated.

This plan, which became known as the Accelerated Pacification Campaign, was initiated on November 1, 1968. It was a program targeted on securing additional hamlets and narrowing the goals to essential military, governmental and political requirements. If the campaign was successful, and the Viet Cong were deprived of free access to these selected hamlets, then development programs would follow in the coming months. The military aspects of the campaign required inserting Vietnamese forces firmly in insecure hamlets and maintaining them at all costs. The campaign was met with instant and strong resistance by the Viet Cong, but the government forces generally held their ground. They received support in many areas from U.S. military units. So impressed were Vietnamese and American officials associated with pacification that the 1969 pacification program was modeled after this large scale 1968 experiment.

Another significant development materialized in 1969 which had been in the making for several years. USAID officers, some of whom had by then spent many years in Viet Nam, concluded that pacification and development efforts would be better directed at the larger village level than at the hamlets. There were several major reasons for this.

At this point, the term "pacification" began to narrow in meaning

241

as it was used by MACV. The Accelerated Pacification Campaign emphasized the need to bring military security to a given area, as a prerequisite to undertaking development activities. As terminology changed, "pacification" became associated with the security aspects of the rural effort and "development" referred to those civil efforts which generally fall in the rural development sphere. The Central Pacification and Development Council possessed a name which lent itself to this concept of linking the two processes together but designating separately the military and civil aspects of the program under the two terms of pacification and development. The annual planning exercise for rural areas resulted in a document called the Community Defense and Local Development Plan, which further defined pacification as the military and development as the civil phase of the overall effort. And the operations that followed clearly indicated the importance of close coordination between military and civil efforts with the success of the former serving as a sine qua non to successful implementation of the latter. The success of the experimental 1968 Accelerated Pacification Campaign which stressed the pacification aspect was cited as the proof of that axiom.

During the 1960s the U.S. had attempted to develop a balance between its support to regular military efforts of the GVN and those efforts which were generally grouped under pacification. As a result, by 1968 much of the U.S. military and civilian advisory effort had been targeted on the latter. The Vietnamese, culminating with their mobilization order of 1968, had also shifted a large segment of their assets to pacification.

292

The U.S. was concerned with another problem: the leverage of the U.S. field advisor. A.I.D. province representatives had developed a limited leverage on province governments through their control of counterinsurgency commodities as well as their ability to influence allocation of pacification funds to the provinces. Military advisors had fewer assets to use. But leverage was multiplied many times in 1968 when President Thieu agreed to allow district level American advisors to grade their counterparts, the district chiefs. The tool which brought this about was the Hamlet Evaluation System (HES), a computerized report which was established during the service of Robert Komer as Deputy for CORDS. The HES was an elaborate measuring device with which the district senior advisor rated the progress or decline of the hamlets in his district by reporting certain key factors, such as enemy and friendly military activity as well as political, economic and developmental conditions. These factors were fed into a computer which produced a printout rating the hamlets from a high of "A", indicating a hamlet to be totally under GVN control and functioning well to "V", indicating a hamlet to be totally controlled by the Viet Cong. There were four grades in between the "A" and "V" indicating degrees of hamlet pacification and development. There were a number of imperfections in the HES, including the fact that district advisors were not always able to get adequate information to prepare it, nor were their judgments uniform throughout the country. But if it did not show precisely the status of security and development in the hamlets, it did at least show the direction, up or down. It also provided a great deal of data on local conditions in the country side.

In 1968, the HES took on a totally new significance. The GVN was

243-

threatening to replace district chiefs whose hamlets did not perform well according to the ratings of American advisors. This decision came as a shock to many province and district chiefs, who found themselves being supervised by foreign advisors. To the Americans, some of whom did not fully understand the policy, the new role came as a mixed blessing. Those who realized the potential of their new power and who stood firm, were able to put a great deal of leverage behind their advice. Vietnamese officials were obliged to follow that advice at the risk of losing their jobs. Other advisors saw the HES as a deterrent to good relations with the district chiefs, their counterparts, and were vulnerable to pressure from counterparts causing HES ratings to be higher than they should have been. But in general, by 1968 the HES became a powerful tool in the hands of U.S. advisors as well as proving useful in measuring the pace of pacification and development efforts. In the long run, it provided more leverage in the military than the civilian areas. The HES continued as an important tool, especially for U.S. advisors, until the cease fire of 1973, when the military advisory effort was terminated. At this point the HES was "Vietnamized" and thereafter operated by the Vietnamese themselves.

The village government historically was the lowest level of government at which some managerial expertise had developed and the lowest level at which taxes were collected. The simple arithmetic of hamlets in South Viet Nam made this lower level of government very difficult to deal with. There were, depending on what method was used to count them, between 10,000 and 12,000 hamlets. The managerial problems for the 44 province governments dealing directly with the hamlets were all but insurmountable.

294

But dealing with 2,100 villages, 35 to 50 in most provinces, provided a workable managerial scheme.

Although the village government had been all but neglected in the years since President Diem discontinued village elections, they somehow managed to stay intact, even though they were not given any significant role in the pacification program.

The groundwork for re-emergence of village governments had been laid in 1967. During that year, in addition to elections for the national President and the General Assembly, the GVN reinstated village council elections throughout Viet Nam. Although elected, village councils had little to do with pacification and development activities since the majority of the local programs were still being operated at the hamlet level independent of the village government by the RD cadre teams. And the cadres were unwilling to share their responsibilities with the village chiefs.

A number of Vietnamese officials felt strongly that the emphasis on hamlet over village governments was detrimental to the goals of pacification. This growing consensus led to the adoption of a pacification plan for 1969 which utilized the village as the basic management level, with hamlet governments serving as sub-managers for the village governments.

Yet another key development, which had been announced in 1968, was the gradual withdrawal of U.S. combat forces in Viet Nam, a process which would impact not only on military activities but on the civil

205-

economy as well. For American advisors it meant the beginning of a Vietnamization program, which would gradually replace Americans serving in operational or semi-operational roles with Vietnamese. The first clear impact of Vietnamization came when the U.S. Ninth Division, stationed in the northern Delta of South Viet Nam, began leaving in August, 1969, heralding the first major withdrawal. Areas of military responsibility filled by the U.S. Ninth were turned over to Vietnamese troops, including installations which had been constructed for the U.S. Ninth. A similar process took place in the advisory area as the total number of advisors was gradually reduced. Their roles were either taken over by Vietnamese employees of the U.S. Government or subsumed into Vietnamese government activities.

The largest single civilian input into CORDS in 1969 remained USAID, which provided not only personnel but funds to support a number of key programs. The military "pacification" segments of CORDS concentrated on promulgating the type of security which had proved so effective in the 1968 Accelerated Pacification Campaign. This included advising on intelligence matters, training and expanding Regional and Popular Force troops who were helping to fill the military gap left by U.S. forces, and in general assisting in placing more population under control of the Vietnamese government. USAID Viet Nam, and its field advisors in CORDS, were involved in the "development" segment which included the refugee program, the Chieu Hoi program, public safety, and a wide range of local development activities in agriculture, education, self help, public works, etc., at the province and village levels, as well as overall assistance to the City of Saigon.

240

As the Vietnamese military forces moved out and secured additional areas in Viet Nam, USAID public safety advisors continued assisting the National Police to reestablish police units in the more secure villages. The increase of police at the village level in turn freed more military forces to move out even further. Thousands of Vietnamese rural dwellers who had become refugees in 1968 and before sensed a feeling of security and moved back to their rural homes. USAID officers assigned to the CORDS Refugee Directorate and to field positions, worked with the Ministry of Social Welfare to execute the Return to Village program, which expanded greatly in 1969. More than 400,000 Vietnamese returned to their original homes in that year.

For rural development in Viet Nam, the major achievement of the year was the shift from hamlet to village administration. From the province and district level, advisors were able to monitor and advise on the development of village level activities.

The Vietnamese Central Pacification and Development Council supervised the total pacification program. The Ministry of Rural Development and its more than 40,000 village-based RD cadre, provided a direct channel to village level programs. The recently elected village governments were given control of small military units to protect themselves and their operations. USAID provided, through the Ministry of Rural Development, a million piasters for each participating village. Regulations for use of these funds were relatively lax and provided a great deal of opportunity for village level decision making. At the

297

province level, more USAID-generated piasters were used to allow province governments to address some of their more urgent needs, e.g. roads, bridges, schools and other facilities. These province level programs were administered by the CPDC.

The village focused rural development program of 1969 represented a major shift from previous efforts. There was a need for village and province, as well as regional and national officials to learn entire new sets of regulations and new concepts of operation. The new program guides were formulated under the direction of CPDC and MORD and moved down to the village level slowly. Funds stagnated for long periods at various levels of government. Province and district governments at times interfered with village control over security and village rights to select projects. And finally, there was the big question of the village governments themselves. Would they, after years of sitting on the sidelines, rise up to the heavy new responsibilities put upon them?

The new programs proved in some part to be as much a training exercise as a development program in 1969. But as the year advanced, key problem areas were detected both by the Vietnamese and their American advisors. Through the mechanism of the CPDC, MORD and the American advisory system, these problems were surfaced as far afield as the village level and brought to the attention of the national government. Adjustments were made in 1970 and in later years which added new dimensions to the programs. Among those problems was the clear need for more training at lower levels. The National Training Center at Vung Tau, which had trained the 40,000-man Rural Development Cadre, was called on

248

to train thousands of village and hamlet officials, and later province officials in the rural operations of the Vietnamese government. Some village officials were even sent abroad to observe other local governments.

In 1970, more attention was placed on local government administration and on province and municipal development. USAID, which had assisted the Vietnamese Ministry of Education for years in construction of elementary schools, concluded that this aspect of A.I.D. operations should come to a close. A large percentage of elementary-age children were in school and the Village Self-Development program was producing a number of village and hamlet schools which was running ahead of the supply of teachers.

Village elections continued in 1970, and were held in 1,000 villages and 3,760 hamlets. In June, elections were held for province and municipal councils, based on new national legislation. These councils served to produce at the province level a group of delegates from the districts, thus providing another channel of expression between the Vietnamese people and their government. USAID provided piasters to allow councilmen to execute their own projects under the direction of the CPDC.

There were 4,000 village and hamlet officials trained at the National Training Center in Vung Tau in 1970 and 41,000 trained in province training centers.

The Ministry of Rural Development continued its decline in usefulness even as village governments became operative again and filled the void for low level management. The MORD field wing, the RD Cadre, once the dominant force in local activities, waned in influence. It still

291

attempted to operate in assisting village officials with programs but its primary duty, which was to serve as a catalyst at the hamlet level, was gone. By 1970 the action had moved to village government.

#### Province-Village Relationships

During the many years of war in Viet Nam, contact between province service chiefs and lower levels of government was minimal. The danger in rural travel and the great press of business in province towns kept GVN officials away from the villages where their programs were executed. This weakness became more apparent after the reestablishment of the village government as a development force, especially since many projects required a degree of technical and administrative assistance from the province level which did not exist at the village level.

This problem concerned the GVN and USAID at the highest levels. In early 1970, the Province Chief of An Giang Province and his American counterpart began experimenting with methods of providing assistance and guidance for village governments from the province level. This resulted in a delivery system for province technical services known as the Province Mobile Assistance Team. It was, in fact, composed of three sub-teams; one dealing with military affairs, one with government administration and the third with development. The teams traveled systematically to each village in the province over a period of months, analyzing programs and progress, making corrections, and solving some problems on the spot. It also recorded the unsolved problems and reviewed them at province level where they were either solved or sent to higher levels if necessary. USAID advisors at the Region 4 (Delta)

300

headquarters of CORDS were so impressed with the results in An Giang that they promoted the idea with the Vietnamese Corps Commander, who ordered all provinces to operate similar teams. The An Giang Province Chief was asked to present this concept at the national level through a series of seminars for province chiefs and other officials. Gradually, the concept spread through most of South Viet Nam and by late 1971 was utilized by the Central Government as a device to provide greater supervision, especially in technical fields, to local governments.

USAID public safety advisors assigned to CORDS at that point, continued to press for a National Police presence at the village level. By the end of 1970, 10,000 officers were stationed in 1,700 of the 2,100 villages of the country. These village police officers provided the needed security in the expanding pacified areas. USAID also began pressing the GVN for an upward revision of the local tax structure in 1971. After developing a series of proposals, which were presented to GVN, USAID officials pressed for action.

CORDS moved to improve local planning during the same year. Its Plans, Policies and Programs Directorate pressed the CPDC for a four-year plan which would allow the GVN to build systematically one year at a time on the accomplishments of the preceding year. The four-year plan was adopted and published with revisions made annually.

The plan required inputs from each of the GVN line ministries as well as inputs from Vietnamese military forces. In addition to serving as a planning document, it served also as a kind of organizational web

which allowed the Prime Ministry to pull the line ministries more and more into the pacification program. It required them to commit themselves to and be accountable for a particular course of action in the rural areas. The ministries reacted at first sluggishly to these requirements, but as the web was tightened their performance became more and more responsive.

#### 1971: The War Subsides

The GVN and U.S. had reason for good cheer by 1971. GVN's national pacification and development program had begun to make its impact on Viet Cong operations. The Viet Cong were becoming less of a menace both militarily and politically. One might begin to see the end of it all, when Viet Cong violence and political intimidation would reach an acceptable level, if not disappear altogether. The GVN presence in the countryside, which had been largely a myth in the late 1960's, was becoming a reality. In many villages national policemen, not soldiers, were keeping the order. Developmental programs at village and province level had evolved into useful adjuncts to the total counterinsurgency program. The village level of government was managing local programs more capably than the hamlets did before them. Province Mobile Assistance Teams were providing adequate supervision and assistance to the villages in many provinces. Nationally, inflation had reached a new low and the possibility of giving more attention to development materialized.

#### Rural Development Cadre Role Revised

However, there were still major unsolved problems. The Rural

Development Cadre groups whose role as substitute government teams had faded with the resurrection of village governments, were basically unemployed by 1971. The CORDS Community Development Directorate championed a new role for the cadresmen as energizers at the village level of CPDC programs. Both the Minister of Rural Development and the Prime Minister's office agreed. As a result, early <sup>in</sup> 1972, MORD's cadresmen were reformed as Village Pacification and Development Teams and ordered to assist and supervise all CPDC programs at the village level. The cadre's deployment had been undergoing transformation for some time. The size of each team had been reduced from 59 men, mostly security troops, in 1966 to 30-man teams. In 1972, they were dispersed throughout 1,800 of the 2,100 villages with as few as three members of the cadre in smaller villages. This new deployment and its accompanying new mission, provided the RD Cadre with more than enough to keep them busy at the village level. It also provided the ailing Ministry of Rural Development with a new lease on life.

Another ministry, the Ministry for Development of Ethnic Minorities (MDEM) operated a Montagnard cadre, known as the Son Thon Rural Development Cadre. Although poorly trained, they were deployed in somewhat the same configuration as the Rural Development Cadre, but located in provinces with a high Montagnard population. Both ministries, MDEM and MORD, emphasized the decentralized nature of their operations by the deployment of their cadresmen, as shown in the late 1973 figures:

	<u>MORD Cadre</u>	<u>MDEM Cadre</u>
Assigned to Ministry in Saigon	158	50
Assigned to Province Headquarters	1,572	327
Assigned to District Headquarters	1,377	none
Assigned to villages	<u>15,916</u>	<u>2,893</u>
Total	19,043	3,270

Village Development Funded Locally

The Village Self-Development Program was operating well enough. But its support still came mostly from USAID generated funds at the national level. CORDS proposed in 1971, that the Vietnamese Government gradually phase this program into local village taxation. At the same time, GVN was informed that the Village Self-Development Program would be phased out of U.S. funding at the end of 1973. The GVN agreed somewhat unenthusiastically with this idea, and published references to it in its annual plans. But it took no active steps to promote the principle of replacing U.S. funds with locally generated ones. The U.S. position remained and on May 21, 1973, the Minister of Rural Development and the Minister of Interior, signed a joint circular address to province chiefs, outlining the steps which must be taken to assure a smooth transition of the village Self-Development Program from national to village-financed funding. In 1971, no village taxes were committed to the VSD Program. In 1972, 60 million piasters were committed. More than 370 million were committed in 1973. In early 1974, all VSD funding was turned over to village governments. Although no tally was made of the 1974 village taxes used for development, it is estimated that at least one or two billion piasters was committed.

### Redirection of Field Advisors

U.S. field advisors were also the subject of redefinition in 1971. Through the years, although they had received general guidance from above, their duties remained somewhat ill-defined. And in some cases, well meaning advisors had lost sight of overall goals in order to address local problems which were not necessarily germane to the central issue of getting local government on its feet. Some field advisors, especially in Military Region II, felt their presence was unproductive, perhaps even counter-productive and questioned the validity of their roles. However, the CORDS regional advisors in Region IV, the Delta, had developed a list of goals and a job description for province development officers early in the year. These goals and the job description were reviewed and revised by other regional officers and by CORDS/MACV and ordered into general use on September 6, 1971. They remained in effect until CORDS was disbanded in 1973.

### Ethnic Minorities Programs Redesigned

USAID had given aid to the non-Vietnamese mountain people of Viet Nam (Montagnard) for some years. Their needs were great, their assets were few and progress was painfully slow. In 1971, a Montagnard, Nay Luette, was named Minister of the Ministry for Development of Ethnic Minorities. Although chronically ill with tuberculous, he proved to be energetic and determined to push programs forward for his people. In his first efforts, he attempted to attack all known problems simultaneously, dispersing his very limited human resources too thinly. After discussions

305

with the Rural Development advisory staff, he narrowed his goals, reorganized his ministry, and concentrated on improving rural development, land reform, education, agriculture and public health in the Highlands. Using the National Montagnard Training Center in Pleiku, a USAID supported project, he developed a series of short term programs to fill the training voids among his people. These programs covered subjects in his specific fields of interest as well as in such areas as literacy training for local officials and courses in conduct of the USAID-sponsored Village Self Development Program, which had been going poorly in the Montagnard areas since 1969. The MDEM continued to concentrate in these areas throughout the balance of the life of the Republic of Viet Nam.

#### The 1972 Communist Invasion

Although the Viet Cong seemed to provide an ever decreasing threat to the South Vietnamese, by early 1972 it was generally agreed that the North Vietnamese Army was preparing a large-scale conventional assault on South Viet Nam. But important questions had to await the arrival of the North Vietnamese Army for an answer: where, and when?

At the end of March, the North Vietnamese, supported by Viet Cong forces, struck South Viet Nam with the first large-scale conventional campaign ever launched in the war. Bolstered by heavy tanks of Chinese and Russian origin, they advanced across the 17th parallel into Quang Tri province and attempted, without success, to reach Hue. From the western border they moved from Laos into Kontum Province where their forward advance was stymied at Kontum City. During this offensive, one

of USAID's most able and renown field officers, John Paul Vann, was killed on June 9th in a helicopter crash between Kontum and Pleiku. Vann, who first served with the U.S. Army in Viet Nam, began his USAID career as province representative to Hau Nghia Province and had been appointed the senior military adviser to Military Region II the year before his death.

Another North Vietnamese thrust in Military Region III placed the province of Binh Long in jeopardy and the province capital, An Loc, was leveled during bitter fighting. But a thrust from Cambodia into the Delta of South Viet Nam proved unsuccessful. There was intense fighting in a number of South Vietnamese provinces. But when the fighting died down, most of South Viet Nam was spared the full brunt of the invasion.

The invasion created a number of civil problems. Of first importance to the CORDS effort was the care of more than a million refugees, most of them in Military Region I. Province advisors were directed to turn their first efforts towards easing the problems of the refugees.

The rural development process was converted of necessity to fit the occasion. After assisting with refugee resettlement, advisors turned their attention towards the decimated local governments and their facilities.

By May, the CVN and U.S. had produced a recovery program to regain ground lost to the enemy and to restore local government and facilities in areas where fighting had destroyed them. There were 245 villages whose governments had been placed out of action by November 1972. In

addition, the province capitals of An Loc and Quang Tri had been destroyed and there had been extensive damage to other province as well as district capitals. Village elections were temporarily suspended to prevent infiltration by the enemy.

The CPDC was placed in charge of recovery by the GVN. Working with this group the CORDS Community Development Directorate, later the USAID Rural Development Division, proposed in June that the GVN take several steps to expedite recovery:

1. Get local governments back into operation.
2. Divert existing ministerial budgets as well as USAID rural development funds to recovery programs rather than await additional funds from undetermined sources.
3. Develop a pilot province program to iron out funding and management problems while waiting for the fighting to die down in other provinces.
4. Use existing rural development funding procedures and managerial processes to manage the programs of recovery.

These steps were taken and the CPDC took the lead in managing rural recovery programs. The exercise also gave the CPDC new insights into the management of rural programs through closer coordination of all available government assets. The line ministries, which several years before had been reticent to cooperate on such joint projects, joined the recovery effort with surprising enthusiasm, committing both funds and personnel to assure the most efficient conduct of recovery programs.

Agreement by the line ministries represented a singular achievement for the Prime Ministry, which had not been able to obtain such a quick and responsive reply in the past. The ministerial response was partly due to the nature of the problem: a crisis brought on by the North Vietnamese Army invasion. But it also illustrated the growing power of the Prime Ministry over the line ministries.

By November, 1973, the number of defunct village governments had been whittled from 245 to 127. From recovery, CPDC moved in 1973 again into rural reconstruction where it continued to operate until Saigon's fall.

#### CORDS Disbanded

On January 27, 1973, a Cease Fire sounded the end of U.S. military participation in the Viet Nam effort. It also heralded the end of MACV's pacification and development operations under CORDS. The U.S. military elements were quickly withdrawn. The Public Safety Division, affected immediately by the Cease Fire Provisions, was withdrawn from Viet Nam. The community (rural) development effort and the war victims effort in CORDS were transferred to USAID on February 1. However, when CORDS was disbanded on March 1, 1973, another office was set up under the Ambassador to carry out field operations in the absence of the military and to monitor GVN activities in the pacification and development area. The Special Assistant to the Ambassador for Field Operations (SAAFO) was appointed. This new office contained 159 USAID positions, 17 of which were in Saigon, 59 at the regional level, and 83 at the province level.

The field employees were subsumed under the operational control of four consulates general which were established in Da Nang (MR-I), Nha Trang (MR-II), Bien Hoa (MR-III), and Can Tho (MR-LV), replacing the former U.S. military advisory commands.

At the time of this organizational change, there were 343 USAID positions remaining in the field effort. Forty-four of them were returned to A.I.D. with the return of the Community Development (10 positions) and War Victims (34) functions. Engineering, logistics and data processing positions in CORDS produced 17 additional returns to USAID. A total of 123 CORDS positions were abolished. SAAFO remained in operation until the fall of Saigon providing a lightly manned field effort which responded to and monitored problems in rural areas. The total number of positions in SAAFO was reduced to 85 in 1974 and remained at that level until the fall of the GVN.

From February 1973 until its deactivation in June, 1974, the Saigon-based USAID Rural Development Division, which dropped to six positions during the year, worked less and less with the field advisors concentrating its remaining resources on dealing with the ministries of Rural Development and Ethnic Minorities and with the Central Pacification and Development Council, which had been redesignated the Central Reconstruction and Development Council. By February, 1974, the Ministry of Rural Development was abolished and its remaining assets placed for administrative purposes under the Ministry of Interior. Its operational control was given to the Central Reconstruction and Development Council.

This, in effect, placed under one command those national assets which provided management to province governments. The remaining RD cadresmen who provided impetus at the village level also were directed by the council.

#### Rural Development Plans For 1974

Although USAID planned to discontinue its separate Rural Development project in 1974, 85 A.I.D. officers remained in the field under SAAFO. And the three elements of the Vietnamese Government concerned with rural development continued in late 1973 to plan for continued development efforts following the general pattern of previous years.

The CPDC, under its new title of Central Reconstruction and Development Council (CRDC), was allocated \$2.75 billion piasters to continue its province reconstruction efforts. The Ministry for Development of Ethnic Minorities was allocated 630 million piasters for continuation of the somewhat narrower interests agreed on between it and USAID. The Ministry of Rural Development, drawing on some years of its experience in rural planning, conducted a year-long exercise in 1973, producing proposals for a number of village development programs, including a continuation of village reconstruction of war-damaged facilities which it had begun in 1972, by reprogramming its own funds. MORD received approval to undertake 18 of these proposals at a cost of 3.8 billion piasters, prior to its dissolution.

Altogether, these specific rural development and reconstruction proposals required 7.3 billion piasters for the calendar year 1974, all

of which were provided by USAID-generated piasters. Then in 1974, the Ministry of Rural Development was merged with the Ministry of Interior and the Central Reconstruction and Development Council. This major organizational change, added to a shortfall of total funds available to the GVN, brought on a re-evaluation of total programming and many of the programs planned were discontinued. This major rural development planning effort on the part of the GVN was its last in a long series of trial and error attempts beginning in 1954 through the ultimate collapse of the government in April 1975.

#### The Shift Towards Decentralization

During 20 years of U.S. support for rural development in South Viet Nam, a number of changes took place which greatly modified the performance of local governments in South Viet Nam.

From 1954 through 1963, village and hamlet governments, already weakened by war, dropped even lower in performance and even visibility to the population as guerilla war increased. There was little contact with the population below the province level, and local government services had virtually come to a standstill.

By 1974, village governments had been resurrected, their officials were largely elected, and they were generating at least a billion piasters worth of public use projects which they themselves funded from local taxes. They were making their own decisions on what to do and how to pay for it.

Province governments were active not only in their own affairs, but in supervising and supporting the development efforts of the villages. And at the national level, there was a reasoned planning process which supported and encouraged local development and partly financed some of the larger projects.

The crowning achievement of the South Vietnamese government in rural affairs emerged in 1973 with the launching of the Administrative Revolution. It can be said that the idea to launch this massive effort at decentralization was purely Vietnamese. But the methods used to define the program, to train the public servants, the very idea of decentralization itself, was the embodiment of those basic principles espoused from the 1950's onward by USAID advisors.

The Administrative Revolution attempted to: decentralize the decision-making process; place village and province chiefs squarely in charge of local operations; discover and eliminate bottlenecks in the archaic GVN system; and increase local government staffs at the expense of the national ministries.

The Administrative Revolution had special significance for the USAID rural development effort in Viet Nam for it offered solutions to problems of over-centralization which had delayed and sometimes foiled rural development programs through the years.

Just as USAID had deployed more than half its personnel to the field by 1968, GVN was determined to deploy a larger number of its 300,000 civil servants in rural areas. Using the RD cadre approach, the GVN chose to garb its civil servants in black pajamas and train them at the

RD cadre's former training center, the National Training Center at Vung Tau.

Much of the early planning for the Administrative Revolution was done by the Minister of Rural Development and by the Assistant Minister, Quach Huynh Ha, who was selected by President Thieu to head the program in June, 1973.

A fuller discussion of this program will be found under the Public Administration section of this report. From the standpoint of the rural development effort in South Viet Nam, it offered the promise of catapulting rural development ahead by permitting local problems to be solved by local governments with a sufficient number of suitably trained staff members. However, before the Administrative Revolution had developed to the point of significantly affecting rural development, it was obliterated in the fall of the Saigon to the Communists. As a developmental process, it must remain in the realm of theory.

The Evolution of Rural Development, 1962-74

Through a process of evolution, South Viet Nam's rural development programs were transformed by 1974 into something quite different than the programs of the early Sixties. In retrospect, the transition from programs based at the hamlet level to those managed at the village level was a relatively simple matter. But the decision to make the change was considerably more complex. The Vietnamese reluctance to develop village governments existed at least as far back as 1954. President Diem was strongly opposed to strengthening village governments.

34-

It was he who suspended village elections in hopes of strengthening the central government. The American push for decentralization was negated by Diem's desires in the opposite direction in favor of stronger central control. The first indication that the GVN would move towards decentralization came when the GVN announced resumption of village elections in 1967. This was followed in 1969 by revamping the entire counterinsurgency program along the lines of more autonomous village governments.

In the final years, the rural development programs which were largely conceptualized by USAID/CORDS officers and funded for the most part by USAID, enjoyed a degree of security from terrorism which made the difference between success and failure. This security was the result of the massive shift of security assets to rural areas by the GVN from 1969 on. The decision to make that shift was brought about in a large part by the influence of CORDS field advisors' recommendations through their channels to the GVN.

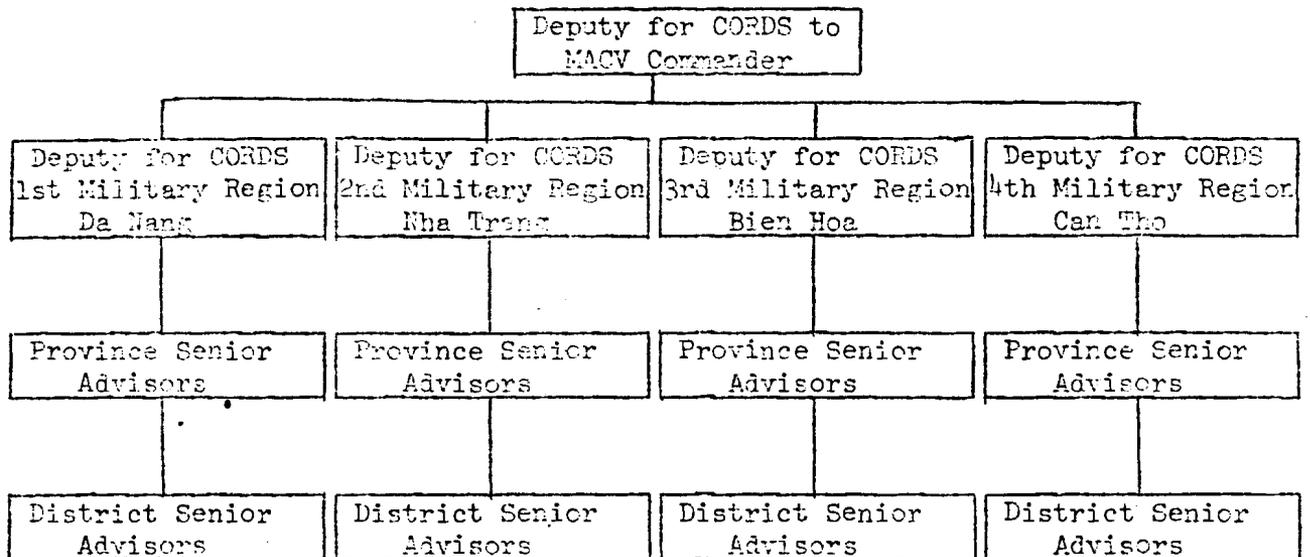
The programs developed a relevance to one another, brought on by the planning requirements to consider the several aspects of the programs including the military and civil aspects. The requirement to plan four years in advance forced into view the realistic prospective time frame required to pacify all of Viet Nam. This, in turn, helped the GVN and its advisors understand better how to deploy its increased military and civil forces more effectively in order to accomplish the whole task.

In spite of the early objections to local autonomy, the GVN had been restructured from the ground up. The early work in hamlets not only

provided the GVN with experience in dealing with local governments but also contributed to the development of a degree of competence among hamlet leaders which proved useful later when these leaders had to respond to the authority of the village government. The village government itself received a great deal of attention from U.S. and GVN officials alike. The province government was addressed at the same time with increasing interest as it became clear that villages needed support and guidance from the province level in order to function efficiently. The relations between province governments and village governments were addressed through the province mobile assistance teams. And, through the CPDC, relationships between the executive office and the line ministries were addressed with resultant improvement in relations between them.

Much of the targeted activity of CORDS field development advisors was concerned with organizational rather than technical problems; of building a government which could communicate down and up and which could manage multifaceted programs spread over a wide geographical area.

As USAID's rural development projects were phased out in early 1974 and funding decreased, the programs it had developed, many of which continued, fell into this overall pattern of developing government institutions which could manage, and in some cases even fund locally, the various development programs. (A description of each program is found in Attachment 2 which follows.)

CORDS Field Organization

Although a part of the Military Assistance Command, Viet Nam, the CORDS chain of authority was usually direct, rather than proceeding through staff channels as it might have. Direction of regional and province advisors usually emanated from the Deputy for CORDS, to the regional deputies, rather than from the Commander, MACV, through the commanding generals of the regions to the regional deputies and province senior advisors.

## I

Summary of Major Programs Which Evolved from Rural Development Activities

As of February, 1974

The preceding section describes A.I.D. activities in the field of rural development through field advisors from 1954 through 1975. Although the programs and approaches changed, the intent of these programs remained basically the same: to bring the Vietnamese people closer to their government by assisting the government in providing normal local services to its people. As USAID closed its rural development activities in Viet Nam, it left the Vietnamese government with a series of programs which produced the management and the organizational structure, as well as a source of funding from indigenous sources in some cases, to provide greatly improved services to its people. Following is a brief description of those programs mentioned throughout the rural development section as they moved out of the USAID advisory orbit in 1974. These programs represent the significant achievements of the USAID rural development effort in South Viet Nam.

Central Pacification and Development Council (CPDC) Programs

The Central Pacification and Development Council (known in 1973 and 1974 first as the Central Reconstruction and Development Council and later as the Central Security and Development Council) represented an institutional breakthrough for the GVN, one which was fostered by CORDS. It represented the last and the most successful attempt at day-to-day coordination of the line ministries in rural affairs and an advanced agency for planning and executing rural programs. Like many other improvements in Vietnamese affairs, it was created to respond to an immediate crisis and its success was built partly on its ability to react thoughtfully to subsequent crisis which were the order of the day in Viet Nam.

Through this agency, USAID advisors assigned to CORDS successfully developed a province management system known as Province Mobile Assistance Teams. These teams, composed of high level province officials, toured each village systematically, reviewing government programs, solving problems on the spot and following up on more difficult problems which must be solved at higher levels. This concept was adopted as a permanent process in of government.

The secondary road system, a key element in the development of Viet Nam, was also improved through USAID's work with the CPDC. Utilizing that office as the allocation agency, a carefully developed system of producing concrete plans at the province level, which were in turn submitted to the CPDC for approval and fund allocation resulted in

### III

an improvement and expansion of the long-neglected secondary road system with highest priority going to the most needed roads. Later, when the North Vietnamese Army launched a full-scale offensive in South Viet Nam in 1972, the CORDS Community Development Directorate (RD Division) approached the CPDC and suggested ways of precipitating a civil recovery movement, using current availabilities. This program was adopted by the Government and in several months the actual reconstruction of rural government facilities began. Within a few more months it had established itself as a viable system for rural reconstruction in South Viet Nam and was given that mission in 1973. Again, this institutional improvement became a standard part of the Government of Viet Nam's operations for post-war reconstruction.

Much of the encouraging movement towards decentralization and greater government civil performance under the Administrative Revolution of 1973-74 could be traced to the precepts offered to the GVN by U.S. field operations from 1962 on. The Administrative Revolution, a massive attempt to decentralize government to lower levels, received much of its stimulation from USAID and the hundreds of CORDS field advisors who served in South Viet Nam's provinces during the war years.

The CPDC managed several key programs directed towards problem solving at the province level. These programs, which have been alluded to in preceding paragraphs and are detailed below, were funded by USAID generated piasters exclusively until 1972 when advisory influence generated

IV

some funds directly from the GVN budget.

The Province Development Fund

In 1969, the Province Development Fund, a counterpart piaster-funded program designed to subsidize projects of provincial priority aimed at "opening up the countryside," was established under CPDC management. Total program funding in that first year amounted to somewhat more than VN\$ 1.4 billion, with about VN\$ 650 million going to secondary roads and bridges, which together with irrigation structures (VN\$ 282 million) made up -- as they were continuously after -- the major part of the CPDC effort. A feature of the CPDC approach, honed considerably with experience, continued to highlight its success as an efficient resources-allocation device in planning at the province level and review at the central level by the interministerial forum.

In 1970, USAID agreed to counterpart piaster funding to subsidize a development program for elected Province Councils. The elections were held in June; the program was funded at VN\$ 1 billion. The rather unfortunate decision was made, at the time, to term this new program the "Province Development Fund" (PDF), and to confer a new appellation upon the preexisting CPDC development program, the National Fund for Local Development (NFLD). The life of this program spanned the years 1970 through 1972. Its intent was to provide the wherewithal for representative Province Councils to respond to their constituents' needs and aspirations, and to foster the Councils' growth into effective political bodies. Although it is impossible to generalize about the 44 provinces

the program did succeed in both aims to a certain extent.

The National Fund for Local Development

As described in the foregoing, NFLD, christened the Province Development Fund in 1969, the year of its inception, gave over that name to the Province Councils in 1970. Henceforward, for convenience, we shall simply term it the "NFLD". NFLD funding throughout the life of the program was as follows: (rounded): 1969: VN\$ 1.4 billion; 1970: VN\$ 2.0 billion; 1971: VN\$ 310 billion; 1972: VN\$ 2.1 billion; and 1973: VN\$ 1.7 billion (this latter, and a large part of the 1972 transfers, went for reconstruction and will be discussed below under that head). NFLD received substantial infusions of DOD-purchased piasters to support the Secondary Roads Program, its largest single element, in 1971, 1972, and 1973.

NFLD, as previously mentioned, featured province-level planning by Province Reconstruction and Development Councils (the term "pacification" was excised from the GVN lexicon at the time of the January 27, 1973, ceasefire agreement) and review of priority project proposals by the Central Reconstruction and Development Council (CRDC) working-level interministerial forum, annually. This methodology tended to assure optimum resource allocation, decentralized planning, and placed focus on province, rather than national or regional priorities. As a management approach, it was speedy and responsive due to the strong and direct line of authority from the Prime Ministry (where the CPDC Coordinating Center -- permanent bureau -- was located) to the Province Chiefs. Summary tables showing NFLD funding and projects are shown in

Tables 1 and 2.

Originally dedicated to the usual wide range of rural development, primarily the land communications, irrigation, education and health infrastructures, NFLD was narrowed to roads, bridges and irrigation structures in 1972, with the lion's share of allocations going to the Secondary Roads Program. DOD contributions to this program came to about VN\$ 4.3 billion, or US\$ 16.4 million, from 1971 to 1973. In addition, there was USAID obligation, in 1970, of US\$ 3.7 million to finance procurement of the so-called "Province Package" construction equipment -- 44 sets of machinery to support the Secondary Roads Program at the Province level. The mix, decided upon by a GVN-US task force in 1970, consisted of a roller, a grader, a tractor with dozer blade, a combination front-loader/back hoe, an asphalt kettle and three 2-1/2 yard dump trucks. The Final items -- 22 graders and 26 tractors -- were contracted for by CLA and expected in country during the last calendar quarter of 1974. All but eight of the remaining 297 items had been issued by the Viet Nam Highway Agency (VHA) as of February 19, 1974.

#### Rural Reconstruction

This effort, which became a regular and successful program of the GVN, grew out of the CPDC response to the NVA offensive of late March, 1972, and employed the NFLD resources-allocation and management system. An added feature was the decision to deal with six-month increments of work in order to keep the problem within manageable limits and buy time to seek out additional financial resources.

Dealing first with the hardest-hit provinces, a series of cycles or phases of reviews of province priority project proposals began in August, 1972. Phase I, funded at about VN\$ 500 million from reprogrammed CPDC and line ministry availabilities, was set in motion in September, 1972, and was followed by five more phases that extended through CY 1973. Including the regular 1973 NFLD program, which was in fact given over almost entirely to reconstruction requirements, some VN\$ 6.7 billion in CPDC availabilities and VN\$ 900 million in Ministry of Rural Development (MORD) Funds had been transferred to the provinces for rural reconstruction as of the end of CY 1973. A significant portent was the fact that the last phase of reconstruction in 1973 was financed from the "President's Fund," an extrabudgetary GVN reconstruction account. This transfer, totalling some VN\$ 1,138 billion piasters, consisted entirely of GVN tax revenues. With trivial exceptions, all previous support for the CPDC Rural Reconstruction program consisted of counterpart and DOD-purchased funds (for secondary roads and bridges) piasters.

The CPDC Rural Reconstruction Program for CY 1974 was funded at VN\$ 2.75 billion counterpart piasters in the Foreign Aid Chapter (FAC) of the GVN budget. Calendar year 1974 province priority road, bridge and irrigation project proposals totalling VN\$ 1.9 billion were approved in a series of CPDC reviews held during September 1973.

#### Province Mobile Assistance Teams

PMATs grew out of an effort to structure regular and fruitful interaction between province government (the lowest level of central government) and the village people. The concept, embodied in the

## VIII

National Community Reconstruction and Local Development Plan, was first applied in 1970 in Military Region 4, and involved structured security, administration and development groups made up from the Sector (military) staff and the province technical service chiefs, making regular, supportive visits to the villages. Basic to the idea was an effective system to secure follow-up on village problems. Flexibility in approach to accommodate to local geography, ethnic differences security conditions and customs was an essential element in PMAT operations.

Wherever it was applied with reasonable seriousness, the concept proved an effective medium of communication between central and local government. Field visits and reportage clearly showed that PMAT employment continued with a reasonable degree of success, nationwide into 1974. During 1973, and more intensively after the ceasefire, the GVN published a series of directives aimed at improving the effectiveness and image of local government, and at creating a closer and more benign relationship with the people. The culmination of this drive to enrich the domestic political ambience was the "Administrative Revolution," involving the delegation of powers to local officials, the diffusion away from Saigon of public servants, and serious efforts to simplify administration. Many of these initiatives specifically called for regular and structured visits by province officials to villages and hamlets. As a result, PMATs, long encouraged as a means for enriching GVN-local government communication, received increasing attention.

325

IX

Village Reconstruction

Village Reconstruction was brought about as a result of the North Vietnamese Invasion of 1972 which dispensed destruction or damage to Village Self Development projects built in previous years. This program was slow in getting started, due mainly to the upset condition of village governments, the fact that people had evacuated many villages, and the slowness of provincial governments in assessing war damage and making funds available to villages to repair or reconstruct projects.

More than 900 projects were finally planned by villages and approved by provincial governments. Funds amount to VN\$ 996,400,000 were allocated by the Ministry of Rural Development to support these projects. By the end of 1973, 817 projects were completed and 108 in process of completion, or 88% completion. Funds supplied by the Ministry of Rural Development to support these projects were derived from funds carried over from the Village Self Development programs of previous years, and the 1972 VSD Budget.

Once the delays in planning and fund distribution were overcome, project implementation progressed rapidly. The rising prices of building materials caused slowdowns in implementation and a reduction in numbers and sizes of some projects. The balance of planned projects, still in progress, were completed early in 1974; but some new projects were developed as a result of later NVA action. The Ministry of Rural Development had VN\$ 300,000,000 in its 1974 budget to support additional projects. Most of the projects under the Village Reconstruction Program were

schools, medical and health facilities, market places and some village roads.

The Village Self Development Program

The Village Self Development Program (VSD) was originated in 1969 as a major part of the pacification plan with the principal aim of "winning the hearts and minds of rural people". This was to be accomplished by government support in funds and technical assistance in meeting the people's felt needs and aspirations in areas of social, economic and political development.

During the period 1969 through 1973, 62,390 public-use projects were completed under this program. The breakdown by categories of projects is:

Education	9,500 projects
Public Health	1,811 projects
Agriculture and Fisheries	14,269 projects
Public Works	31,435 projects
Handicrafts	299 projects
Miscellaneous	3,144 projects

VSD was a multipurpose program. Its goals not only included social, economic and political development but were focused on decentralization of authority down to the village level, increasing the autonomy of village governments and people, increasing the administrative capability of village governments and involving the people in participation in community affairs and in their own development.

XI

The first two years of implementation of the VSD Program were, of necessity, experimental. This was due to several influences which caused delays in getting the program started:

1. Administrative inexperience of newly elected village officials;
2. Indifference on the part of rural people to community activities, outside of the family circle, and people's mistrust of government intentions, due to past experiences in the Self-Help program;
3. Reluctance of province and district government to relinquish authority over and control of funds;
4. Untimely reorganization of the village council structure by the national government;
5. A poor system of communications and dissemination of program information from the central government to village government and the people;
6. Poor training in VSD at the National Training Center in Vung Tau;
7. Frequent program changes and a complicated reporting system.

Started on February 1, 1969, the VSD Program showed practically no results until June of that year. Most of that time was spent in training village officials, forming People's Common Activity Groups (PCAGs), and teaching the people how to organize and carry out village assemblies. During 1969 and 1970 numerous changes in program guidelines were effected through trial and error experience. While many projects were completed during 1969 and 1970, the projects left much to be desired and administration of the program at village and province levels was faulty.

Poor success was particularly evident in income-producing projects, which at that time were implemented by government grants.

By 1971, program guidelines were refined to a point requiring very little change and people and officials began to understand the programs. Reporting requirements were simplified and reduced and income-producing projects but under a repayable loan basis under the newly elected Village Credit Program.

In 1972 the Rural Development Cadre were given responsibility for guiding VSD Program implementation at the village level and for disseminating program information and submitting reports. Very few minor program changes were necessary by 1972.

Most significant was the fact that in 1972, village budgets and people's contributions amounted to only 17% of government's contributions to the cost of VSD projects. In 1973, 82% of the support of VSD projects was furnished by village budgets and people's contributions. While much of this was made possible by the Local Revenue Improvement Program, which increased the amount of local tax revenues, the fact that village people made an effort to contribute to its implementation was significant. In 1974, all funding for VSD came from village budgets and people's contributions. Village Self Development had become a fixture in the development process in Viet Nam. A summary of national and local funding for village projects is shown in Table 3.

XIII

The Village Credit Program

In 1970, the idea of putting income-producing projects on a loan instead of a grant basis was conceived and plans to put the program into implementation were worked out - calling for an initial funding of VN\$ 450 million from U.S. counterpart funds, contributions from village budgets and matching funds from the Agricultural Development Bank (ADB). As delays in signing the Program Agreement were experienced, it was not until March 1, 1971 that the program got underway. It was included as part of the 1971 program in which up to 50% of villages' VSD allocation could be put into the Credit Program by vote of Village Assemblies, and matched by ADB. This fund was to become a revolving fund, after repayments were made and ADB's matching funds were withdrawn.

Loans to individuals were to be approved by a Village Credit Committee consisting of the Village Chief, Agriculture Commissioner, Finance Commissioner, one member of Village Council and one representative of the people. One RD Cadreman was to serve as secretary without vote. Once a loan was approved by the Village Credit Committee it was referred to the Provincial ADB for final approval and disbursement of the loan.

Loans were limited to VN\$ 50,000 per family at 18% annual interest. This was later changed to 20% interest and the loan limit raised to VN\$ 80,000. Income from interest on loans was to be divided thus: 10% to ADB, 6% to the village treasury and 4% to members of the Village Credit Committee. Loans required no collateral from the borrower but village budget contributions and Ministry of Rural Development VSD fund

allocations served as collateral to guarantee ADB matching funds.

In the first three years of this program, VN\$ 3,990,817,908 was loaned to 176,705 borrowers, 87% of 1970-71 loans were repaid, and 74% of 1972 loans were repaid. Of past due loans, 65% were in the heavily war-damaged provinces and provinces hard hit by the typhoons and floods of 1973.

An additional amount of VN\$ 2 billion from A.I.D. generated piasters went into this program in 1974. These additional funds went into a Special Credit Program, confined to certain villages with a 100% repayment history on past loans. Other villages continued with the regular Village Credit Program using funds already in the revolving fund, village budget contributions and ADB matching funds.

#### Rural Development (RD) Cadre Activities

July 1, 1969, support of the RD Cadre Program was assumed by the Department of Defense. At this time the basic goals of the cadre were redesigned and the cadre were tasked as organizers and trained for achievement of the following objectives while serving under the supervision of the Village Chief:

1. To inhibit the enemy activities of propaganda, recruitment and tax collection.
2. To know the people of their village well and distinguish pro-GVN, anti-GVN and the apathetic, and to bring pressure on the latter two; also to recruit and train the pro-GVN as Popular Self-Defense Forces.

3. To ascertain the local power structure, to assist in political organizing, to aid with arrangements for village elections and to evaluate and report on public opinion.

4. To assist in economic development.

Early in it was realized that the RD Cadre needed specific training and improved guidance to provide needed impetus to the various rural development programs of the Community Defense and Local Development plan. Training programs at Vung Tau and the province training centers were re-organized and directed toward economic development goals. The Cadre were redeployed into smaller village teams and in many cases operated individually at the hamlet level. Cadre were also trained for and assigned specific roles in land reform, VSD, rural credit, urban development, information and village administration.

In 1974 the Cadre were deployed in 1,634 villages with administrative groups at the province and district levels. The RD Cadre strength peaked at 48,804. A phasedown agreement for U.S. support had been negotiated in 1970 providing for a 25% annual reduction in support until a zero support level was reached as of June 30, 1974. The GVN picked up the support costs as the U.S. phased down

Through the VSD program the Cadre assisted in the construction of over 6,000 classroom, 400 medical facilities and 5,000 meters of bridges, all in all the VSD projects during the four years 60,000. These been high impact projects greatly needed by the villages. The cadremen performed numerous reporting and analysis

functions which were of value in the management program. They handled the village mail service and the management of many refugee programs and reconstruction programs. They participated in village improvement projects financed by local revenue. U.S. Government support for the RD Cadre from 1969 until termination of support, June 30, 1974, amounted to approximately 16 million dollars.

#### Ethnic Minorities

In 1958, Ethnic Minority populations in the Highlands of South Viet Nam rebelled against what they felt was a threat to destroy them and their culture. In the negotiations with the South Vietnamese government that followed, the Ethnic Minority leaders sought guarantees to leave their people free to preserve their languages and customs while granting them opportunities for greater participation in the nation's political life and for more direct control over the Highland administration. In addition, they wanted to implement social and economic activities to raise the level of their society and they wished to emphasize their rights to hold clear title to the land they farmed.

Recognizing that there was a Montagnard problem, the government began to coordinate a series of agriculture, social welfare, land reform and multifaceted training activities with American advisors in order to gain needed political and military support from the Highlanders. By 1964, they set up a Directorate of Montagnard Affairs as part of the Ministry of National Defense. A short time later, this Directorate was transferred to the Prime Ministers office. By 1966, it was redesignated

the Special Commissariat for Highland Affairs under a Highlander, Paul Nur and, in 1967, it became the Ministry for the Development of Ethnic Minorities (MDEM) with Nur as its first Minister. The Ministry provided a focal point within the government for monitoring assistance to the Ethnic Minorities groups and it also provided a safety valve for tribal people through which they could air complaints and receive some form of assistance, even nominal, without resorting to armed insurrection.

It was not until mid-1971 that MDEM became well-enough organized and staffed to be able to function with some degree of self-sufficiency. Trained cadre teams, working under the Ministry's supervision, built hundreds of school classrooms and maternity-dispenseries, and assisted with secondary roads and bridges. They taught literacy classes, served as agriculture extension agents, assisted in the implementation of land reform programs, advised Village and Hamlet Chiefs on administration, and handled public information dissemination on all program activities.

From 1971 on, the Ministry and its USAID advisors concentrated on these areas of interest:

1. Interministerial Coordination - With continued assistance from American advisors, interministerial coordination was effected with the Ministries of Education and Agriculture as well as with the Central Security and Development Council of the Prime Ministry. This aided and abetted the implementation of project activities initiated in education, agriculture and other development areas.
2. Agriculture - By the beginning of CY 1974, the first comprehensive

## XVIII

Five Year Agriculture Development Plan for Montagnards was completed by MDEM, with major advice and assistance from an A.I.D. contract advisor. The draft plan served as a guideline for the long range program of Highland development that aimed at reaching the goals of self-sufficiency and self-strength.

3. Cadre - Concerned utilization of Son Thon Rural Development (STRD) Cadre members in multifaceted technical and administrative areas developed a much greater MDEM capability in satisfying the needs of people at village and hamlet levels. STRD Cadre played tangible roles in agriculture, education, public health, social welfare, public information, and other project activities.

4. Village Self Development - Non-existent in the Highland area during 1969, VSD projects increased markedly by end-1973 and early 1974. On advice of USAID advisors, this program was transferred from the Ministry of Rural Development to the MDEM in 1973.

5. National Montagnard Training Center Pleiku (NMTC) - From 1971 on, NMTC gave in-field training to Highlanders on the wide ranging subjects of public health, cadre team work, agriculture development, literacy, village and hamlet administration, village self development, mass education and other parallel areas of responsibility. Over 6,000 Highlanders were trained during CY 1973. Training courses were opened in carpentry, mechanics and masonry to further upgrade the knowledge and skills of the Highlander population in 1974.

6. Education - Many of the Montagnards' problems hinged on their lack of basic education skills. Most of them could not read or write

335

either Vietnamese nor their own language. In fact, only several of the 30 languages and dialects had a written form. Progress was very slow. However, enrollment figures for primary and secondary students did increase. From 1969 to 1974 elementary enrollment rose from 37,887 to 60,740 and secondary enrollment rose from 2,248 to 9,407, partly due to the use of boarding schools which were funded by USAID. There was no record of Montagnard university students in earlier years but by 1974, 301 Montagnards were enrolled in universities.

7. Land Reform - At least on paper, the Montagnard land reform program progressed from 1970 through 1974. The Ministry for Development of Ethnic Minorities and the Ministry of Land Reform and Agriculture launched a joint effort to popularize the program in 1973. In excess of 1.7 million hectares of land were set aside in two major programs. But MDEM believed that the actual possession of the land by the Montagnards was being inhibited both by Vietnamese incursions and by poor security conditions. The reader is referred to the separate sector description of land reform in this report for further details.

Results of USAID Budget and Advisory Support

MDEM's budget, financed by A.I.D.-generated piasters, increased annually, as follows: FY 1971 - VN\$ 50 million; FY 1972 - VN\$ 180,845,000; FY 1973 - VN\$ 350 million; and FY 1974 - VN\$ 630 million. In corresponding fashion, STRD Cadre experience and training allowed them to assume much greater training and administrative responsibilities, the National Montagnard Training Center Pleiku facilities improved markedly,

boarding schools began to improve and Village Self Development activities increased sharply in FY 1974. Mass education and literacy training increased, and administrative planning improved.

CPDC DEVELOPMENT PROGRAMS  
SECONDARY ROADS CONSTRUCTION REPORT  
1 9 6 9 - 1 9 7 4  
NATIONAL FUND FOR LOCAL DEVELOPMENT, AND RECONSTRUCTION \*

<u>YEAR</u>	<u>ROAD**</u> <u>(in kilometers)</u>	<u>BRIDGE</u> <u>(in meters)</u>
1969 (NFLD)	396	4,431
1970 (NFLD)	773	2,352
1971 (NFLD)	1,247	5,117
1972 (NFLD)	381	1,243
1972 (Reconstruction)	254	828
1973*** (Reconstruction)	2,014	6,984
1974*** (Reconstruction)	363	1,243
<u>TOTAL NFLD</u>	<u>2,797</u>	<u>13,143</u>
<u>TOTAL RECONSTRUCTION</u>	<u>2,631</u>	<u>8,965</u>

\* During 1972, both the name and the purpose of the National Fund for Local Development were changed to include reconstruction, in order to respond to the damage done during the communist invasion of that year.

\*\* Major repair, rehabilitation and new construction.

\*\*\* Estimated.

February 22, 1974

Source: Rural Development Division/ADLA/USAID, Viet Nam

CPDC DEVELOPMENT PROGRAMSIRRIGATION FUNDING AND ACCOMPLISHMENTS SINCE 1969NATIONAL FUND FOR LOCAL DEVELOPMENT AND RECONSTRUCTION

<u>YEAR</u>	<u>HECTARES</u>	<u>FUNDS (VN\$000)</u>	<u>VN\$/Ha</u>
1969	41,373	232,000	5,610
1970	53,500	337,319	6,305
1971	51,906	520,800	10,034
1972	89,988	528,800	5,876
1973	28,065	266,000	9,478
1974	31,555	719,000	22,786

EDUCATION AND PUBLIC HEALTHSECONDARY CLASSROOMS

<u>YEAR</u>	<u>Classrooms</u>	<u>Funds (VN\$000)</u>	<u>VN\$/Classroom</u>
1969	250	145,000	580,000
1970	224	138,413	617,920
1971	146	144,040	986,580

MATERNITY-DISPENSARIES

<u>YEAR</u>	<u>Number</u>	<u>Funds (VN\$000)</u>	<u>Unit Cost</u>
1969	55	121,400	2,210,000
1970	49	115,500	2,357,140
1971	59	121,135	2,053,140

Prepared February 22, 1974

Source: Rural Development Division/ADLA/USAID, Viet Nam

## PROGRESS OF 1969, 1970, 1971, 1972, 1973 VILLAGE SELF DEVELOPMENT PROGRAMS

As of Feb. 28, 1974

YEARS	PROJECTS			Allocations	Expenditures	Village Budget	People's Contribution	Number of Man Days Labor
	Planned	Completed	In Progress					
1969	26,646	26,447	199	1,668,350,098	1,632,296,857		300,705,141	824,340
1970	21,063	16,430	4,229	2,205,206,581	1,855,694,464		829,837,613	946,110
1971	11,074	9,044	1,929	1,937,309,659	1,662,370,321		407,717,717	838,308
1972	5,492	5,291	283	1,039,827,760	960,887,020	60,654,118	202,370,755	507,092
1973	3,384	3,133	341	623,190,394	574,949,777	379,548,333	167,654,990	296,366
TOTAL 5 yrs	67,649	60,345	6,881	7,473,884,492	6,686,198,439	440,202,451	1,908,286,216	3,412,216

Source: Ministry of Rural Development, March, 1974