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Release 2010/04/12 :
CIA-RDP85T00875R00170002

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CIA/OER/IM 71-188 DOC/SER

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DIRECTORATE OF
INTELLIGENCE

Intelligence Memorandum

The Economic Situation In South Vietnam

Secret

ER IM 71-188
September 1971

Copy No. 211

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CENTRAL INTELLIGENCE AGENCY
Directorate of Intelligence
September 1971

INTELLIGENCE MEMORANDUM**THE ECONOMIC SITUATION IN SOUTH VIETNAM**Highlights

1. The government plans to implement a number of major economic reforms immediately after the presidential election. These include devaluation, tariff and domestic tax revisions, and a pay increase for government employees. To lay the groundwork for these reforms, some important monetary measures were taken last month.
2. For the second consecutive year, there was a substantial increase in Vietnamese agricultural production. The 9% growth in output in 1970 was due mainly to sizable gains in rice and rubber production.
3. Price increases in Saigon have accelerated somewhat in recent weeks. Prices rose about 5% between the end of July and mid-September, compared with only 4% during the first seven months of the year.
4. The money supply, which was stable from January through April, increased almost 5% during May-July. The growth of private sector credit has been a major expansionary factor. The recent monetary measures should offset this tendency.
5. After hitting an 18-month low of 347 piasters per dollar in late August, the black market price of dollars in Saigon rose to 361 piasters by mid-September. The turnaround probably reflects uncertainty surrounding the upcoming election.
6. Charts on foreign exchange reserves, money supply and prices, import licensing, gold and currency prices, and the government budget follow the text.

Note: This memorandum was prepared by the Office of Economic Research.

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7. For some time, the Vietnamese government has been formulating a major economic reform package to be implemented after the presidential election. To assure that the economy is on an even keel for these reforms (some of which may create inflationary pressure), the government took significant monetary measures in August. More recently, President Thieu has tentatively approved the timing and substance of the post-election measures, which will be much broader in scope. They are designed to stimulate economic development, improve morale of government employees, and increase government revenues.

8. To reduce inflationary pressures over the long run, the government last month placed greater restrictions on loans and raised interest rates on savings. The ratio of loans to savings and time deposits for commercial banks was lowered from 70% to 65% and the ratio for demand deposits from 50% to 40%. Interest rates on treasury bills were increased two to three percentage points, depending on the length of maturity. For example, the annual interest rate on a 3-month bill was raised from 12% to 15% and on a 12-month bill from 18% to 20%. On 1 August, commercial banks also increased interest rates on savings and time deposits. Ordinary savings deposits now earn 12% rather than 10% per year. Interest rates on 3-month and 12-month time deposits were raised from 14% and 20% to 16% and 21%, respectively. The measures should slow the expansion of private credit, which already has increased 20 billion piasters, or twice the amount projected last spring for all of 1971.

9. Thieu's economic advisers apparently feel that strong economic measures can more easily be taken while the country is still absorbed in the turmoil of the presidential election. Thus much of the reform package is scheduled to be enacted immediately following the 3 October balloting. The major features are (a) devaluation, (b) a government wage increase, and (c) new, simplified tariff and domestic tax schedules. These provisions have been agreed upon, but some of the specific details probably will not be firmly settled until closer to the date of implementation. Almost all of the measures except domestic tax reform apparently can be enacted without legislation, but the government plans to ask the National Assembly for ex post facto sanction of tariff reform and a change in the official exchange rate.

10. According to the most recent reports, the planned reforms affecting foreign trade and finance will maintain, at least temporarily, the

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existing multiplicity of effective exchange rates. For most transactions the piaster will be devalued from the current rates of 118 and 275 to 400 piasters per dollar, or even above the current black market rate. The 400 rate will apply to exports⁽¹⁾ and all government-financed imports (about half of total imports). It also will apply to invisible transactions, including purchases of piasters by American personnel in Vietnam. Imports financed by the United States under the Commercial Import and Food for Peace Programs will come in at the rate of 250 piasters as opposed to the current rate of 118 piasters per dollar. US government purchases of piasters for official use probably will remain at the official exchange rate of 118 piasters per dollar at least until the end of the year. By then, Vietnamese officials hope to have National Assembly approval for changing the official exchange rate to 400 piasters per dollar.

11. The increase in the cost of imports resulting from devaluation will be offset to some extent by a new tariff schedule that will reduce taxes on all imports. In fact, a large portion of total imports will be tax-free once the reforms are enacted. A simplified tariff schedule - with five rates ranging from 0% to 200% - will replace the existing multi-rate customs and austerity taxes. Until it proves possible to pass tariff legislation to this effect, the new schedule will be enacted through subsidies. Protection for domestic producers will be provided by a perequation tax of up to 25%, which will be granted only upon review of individual applications.

12. Despite the reduction in import taxes and the possible decline in total imports because of devaluation, government revenues from imports are expected to increase. This is because revenue from exchange rate margins⁽²⁾ will displace some of the customs receipts, and collection of revenue through the banking system is much easier than through the customs bureau, which has been notoriously corrupt. In addition to lessening tax evasion, a simple tariff schedule with lower rates could be a useful first step toward bringing domestic and foreign prices into closer alignment and encouraging a more rational resource allocation.

13. Other anticipated measures affecting imports should eliminate restrictions that lead to smuggling and graft. Import prohibitions - mainly on luxury goods - will be lifted in most instances. The general licensing

1. An exchange rate of 350 piasters per dollar already is in effect for most exports as a result of the government's move last June to stimulate exports by granting a 75 piaster subsidy.

2. The exchange rate margin, i.e., the difference between what the central bank pays for dollars and what it sells them for, is the government's source of revenue from the banking system.

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system that was introduced in June will become the rule for all government-financed imports, except a few bulk commodities. This system greatly simplified import procedures and reduced opportunities for graft by licensing officials.

14. A pay raise for government employees has been a likely possibility for several months. Now that Thieu is running unopposed, he apparently has decided the pay increase can wait until after the election, when it could offset some of the unfavorable impact of devaluation. The scheduled pay raise will increase the government payroll 20%. Employees' base pay will be raised, and for the first time there will be combat pay allowances for infantrymen and incentive allowances for such civil servants as tax collectors and police.

15. On the domestic tax front, the government apparently will submit a series of proposals to the National Assembly for simplifying and revising various indirect taxes. The legislature already is considering a revision of the income tax.

16. Should these various proposed reforms occur as scheduled, the Vietnamese government will have introduced its sixth major economic policy package within the past 12 months. Action began in September 1970 with the interest rate reform and was followed in October by a partial devaluation, advance deposits on imports, higher official rice prices, and a government pay increase. In March 1971, rice prices were again raised, some import taxes were increased, and interest rates on treasury bills were substantially increased. Finally, the general licensing system for imports was instituted in June, and the measures described above affecting savings and credit were taken last month.

Agricultural Production - 1970

17. Following a 12% increase in 1969, agricultural production in South Vietnam rose 9% last year. This substantial growth was largely the result of sizable gains in the two major crops - rice (12%) and rubber (18%). Unlike 1969, livestock production apparently increased very little in 1970. The number of hogs grew only 2% and the number of chickens declined 4%. The total cultivated area increased 3% in 1970 as a result of a like increase in the area planted to rice. The area planted to crops other than rice held steady after declining for six years in a row.

18. According to statistics available from the Ministry of Agriculture (see the table), there also were impressive increases in the output of crops such as fruit (8%) and coconuts (20%). Both rubber and sugar cane production rose for the first time in many years, although output still was

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Output of Selected Agricultural Products

	Thousand Metric Tons ^{a/}			
	1964	1968	1969	1970
Rice (paddy)	5,185	4,366	5,115	5,716
Sweet potatoes	301	235	226	220
Manioc	289	260	234	216
Corn	46	32	31	31
Peanuts	36	32	34	32
Fruits	526	420	440	472
Vegetables	108	193	235	218
Coconuts (million nuts)	141	111	98	118
Sugar cane	1,055	426	321	336
Tobacco	7	8	8	8
Tea	5	5	5	5
Coffee	3	3	4	4
Rubber	74	34	28	33

a. Except as noted.

much less than half the prewar level. The decline in output of crops such as sweet potatoes and manioc, however, continued in 1970. As farmers switch to more profitable crops, this trend is likely to continue.

19. The most surprising statistic is that showing a decline in vegetable production. Output of vegetables more than doubled between 1964 and 1969, but declined 7% in 1970. This decline occurred despite a sizable increase in planted area. There is no ready explanation for the sharp decline in yields, but bad weather may have been a factor.

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20. The Directorate of Fisheries has reported a record high catch for 1970. The marine and fresh-water fish catch increased 24% in 1970 to 577,000 metric tons. The number of fishermen rose about 14%, and the expansion and modernization of the fleet continued.

Prices

21. Saigon retail prices rose 2% during the two weeks ending 13 September, bringing the increase for the year to 8.7%. Reflecting an acceleration in price increases, the USAID index rose about 5% between the end of July and mid-September, compared with only 4% during the first seven months of the year. At this point, it is difficult to pinpoint the reasons for the acceleration, but there have been indications that concern over political events has led to some hoarding. The only substantial price changes have occurred for vegetables, and these probably are at least partly the result of seasonal factors. During the week ending 13 September, vegetable prices rose as much as 50% in some cases and declined as much as 14% in others. Continuing a slow but steady increase that began in April, rice prices rose 2% during the week. The price of the grade of rice reported in the USAID index increased about 13% between March and mid-August and probably has risen another 5% or 6% since then. Paddy prices, which reportedly have increased even more during the period, are expected to drop when the harvest gains momentum late this month.

22. Unlike the general price index, the USAID index for imported goods has been quite stable in recent weeks. During August it rose less than 1%. Almost all of the 11% increase in the index this year occurred during the first four months.

Money Supply

23. The money supply increased another 1% in July following a 3% increase the previous month.⁽³⁾ The money supply is now 16.1% greater than at the end of 1970. Although it has increased only 4.6% since the end of January, all of that increase occurred during May-July. Since January, credit extension to the private sector has been a more significant factor in expanding the money supply than the financing of government operations. Hence, the government recently acted to tighten credit to the private sector (see paragraph 8).

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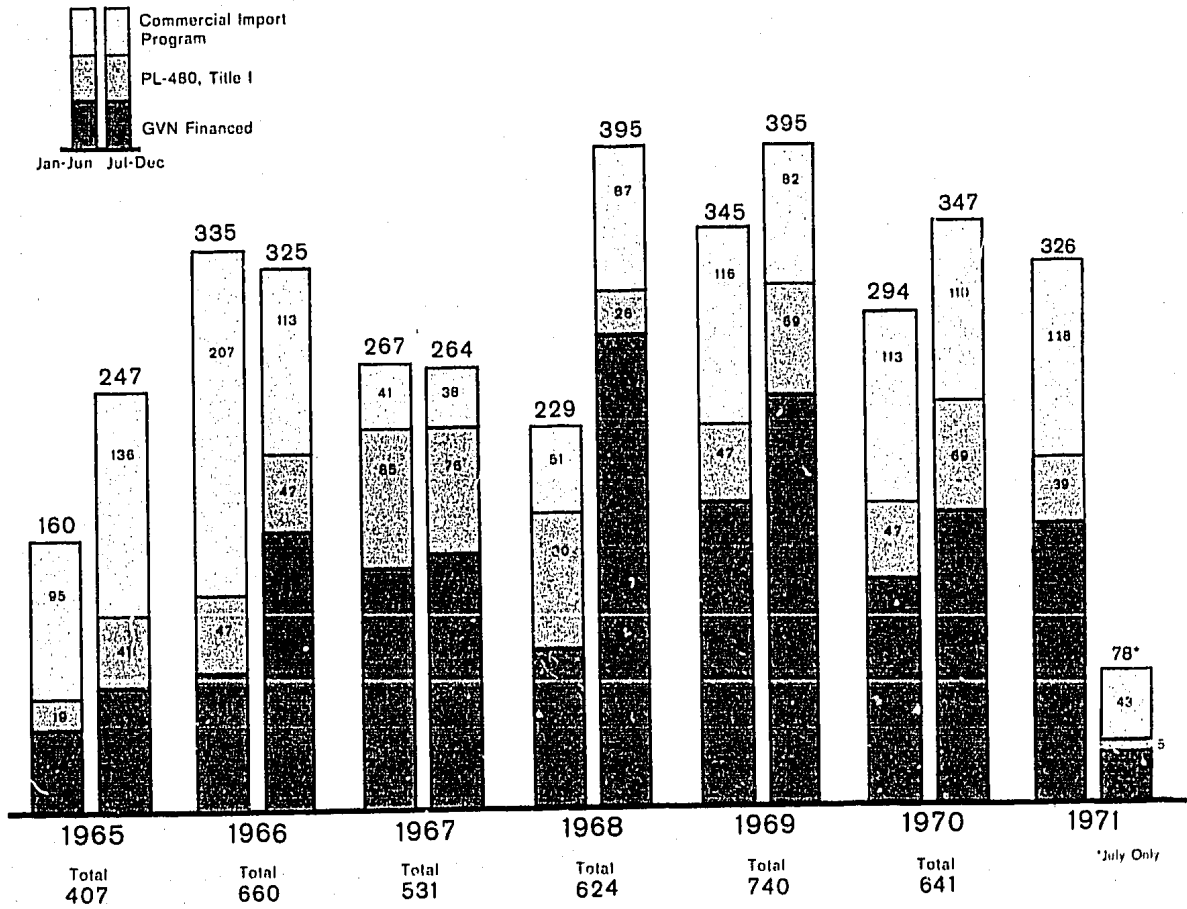
Currency and Gold

24. The black market rate for dollars in Saigon hit an 18-month low of 347 piasters per dollar in late August, but by 13 September it had risen to 361. Although the August low may have been influenced by the economic measures taken in the United States, the value of the piaster had been rising for several months as a result of factors such as a government crackdown on smuggling and the growing confidence in the economy. The turnaround in the value of the piaster during the last few weeks is probably due more to domestic unrest surrounding the October presidential election than to any other factor. Reflecting no particular trend, the price of a dollar's worth of gold leaf stood at 498 piasters on 13 September as compared to 490 on 9 August and 500 on 23 August. The rate for MPC (scrip) has remained below the legal rate of 275 piasters per dollar since February.

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IMPORT LICENSING

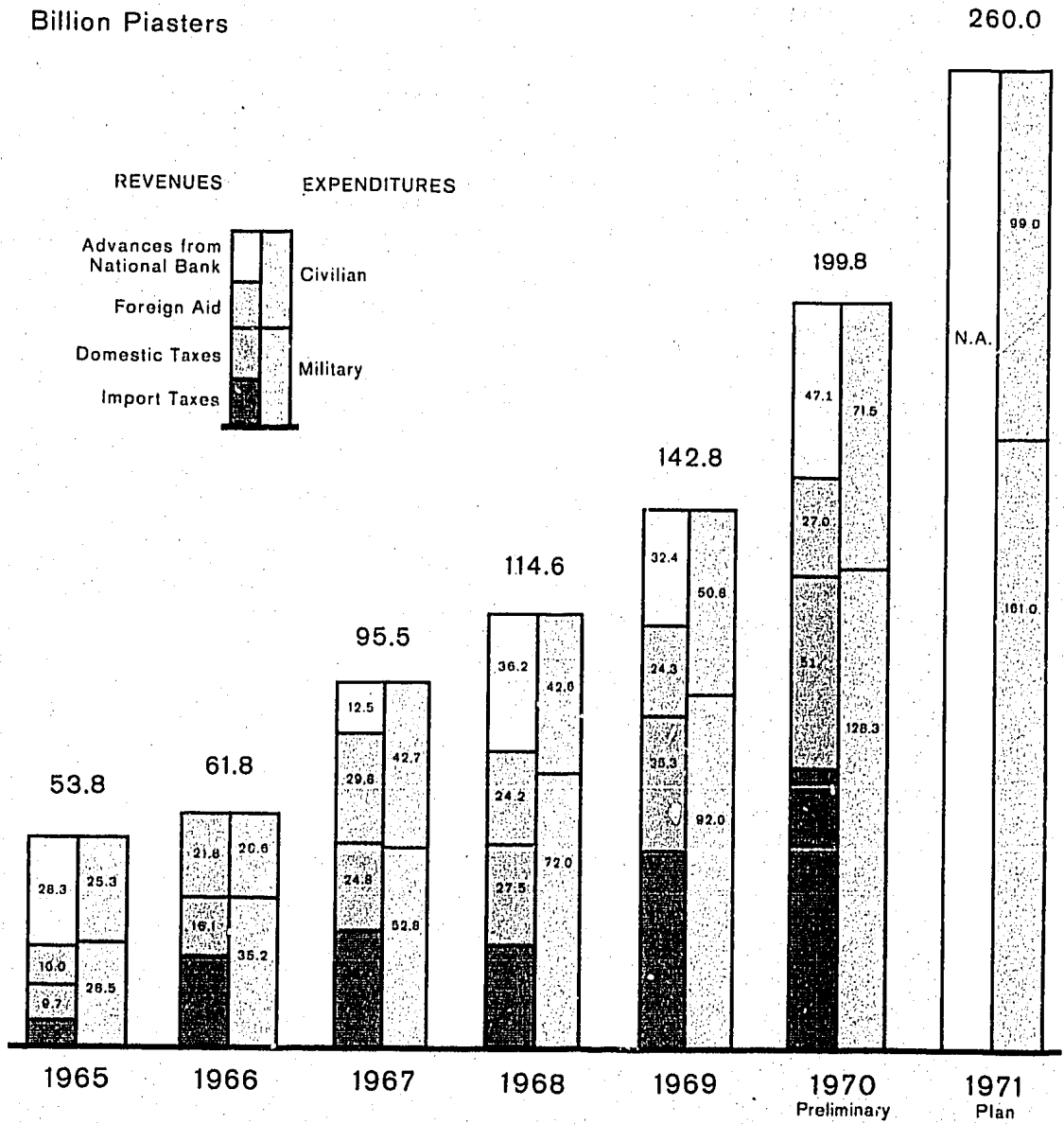
Million US Dollars



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GOVERNMENT BUDGET *

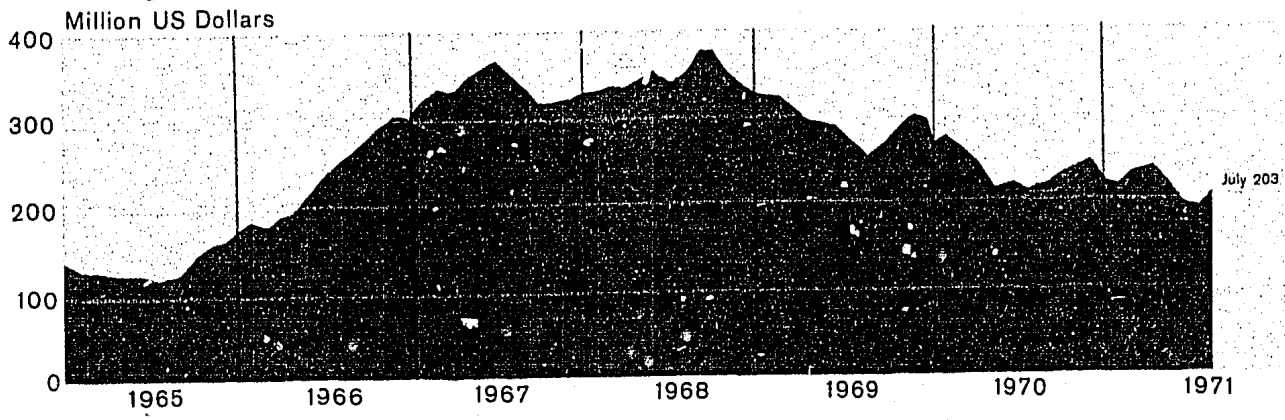
Billion Piasters



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*Data include extrabudgetary revenues and expenditures

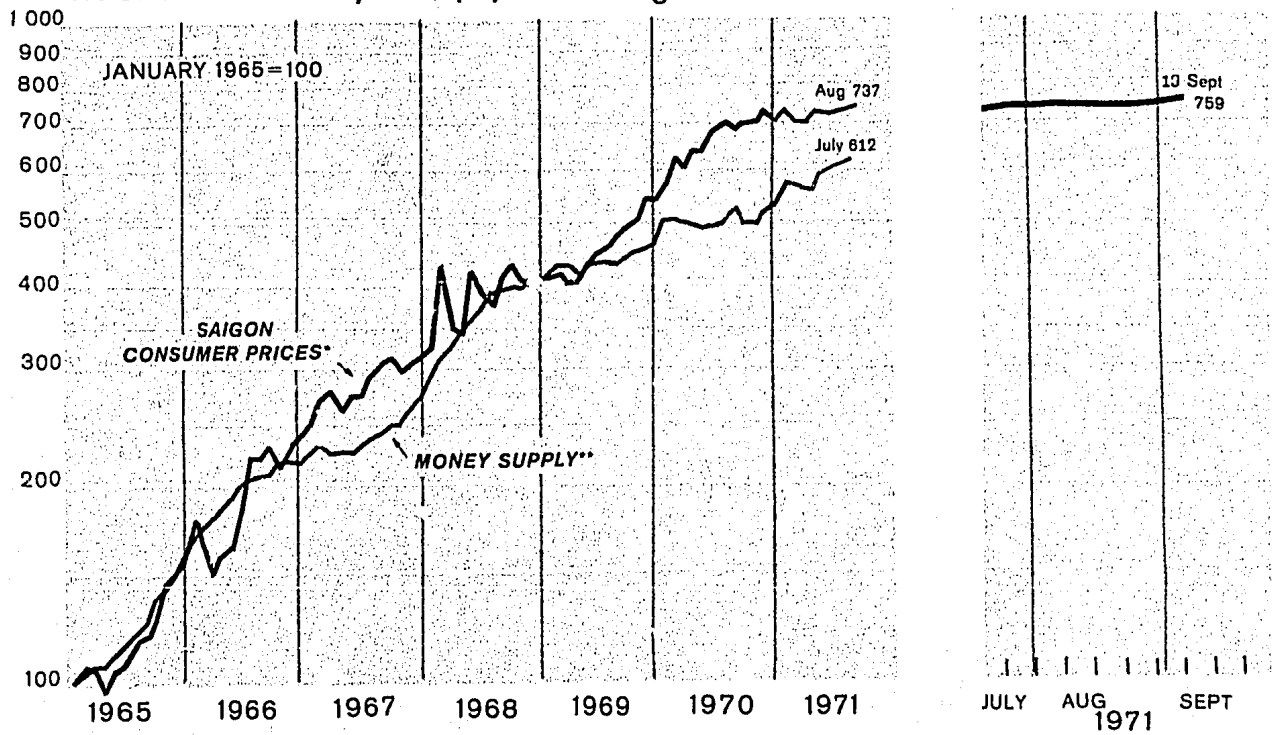
SOUTH VIETNAM Foreign Exchange Reserves*



*Excluding holdings of commercial banks

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SOUTH VIETNAM Indexes of Money Supply and Saigon Consumer Prices

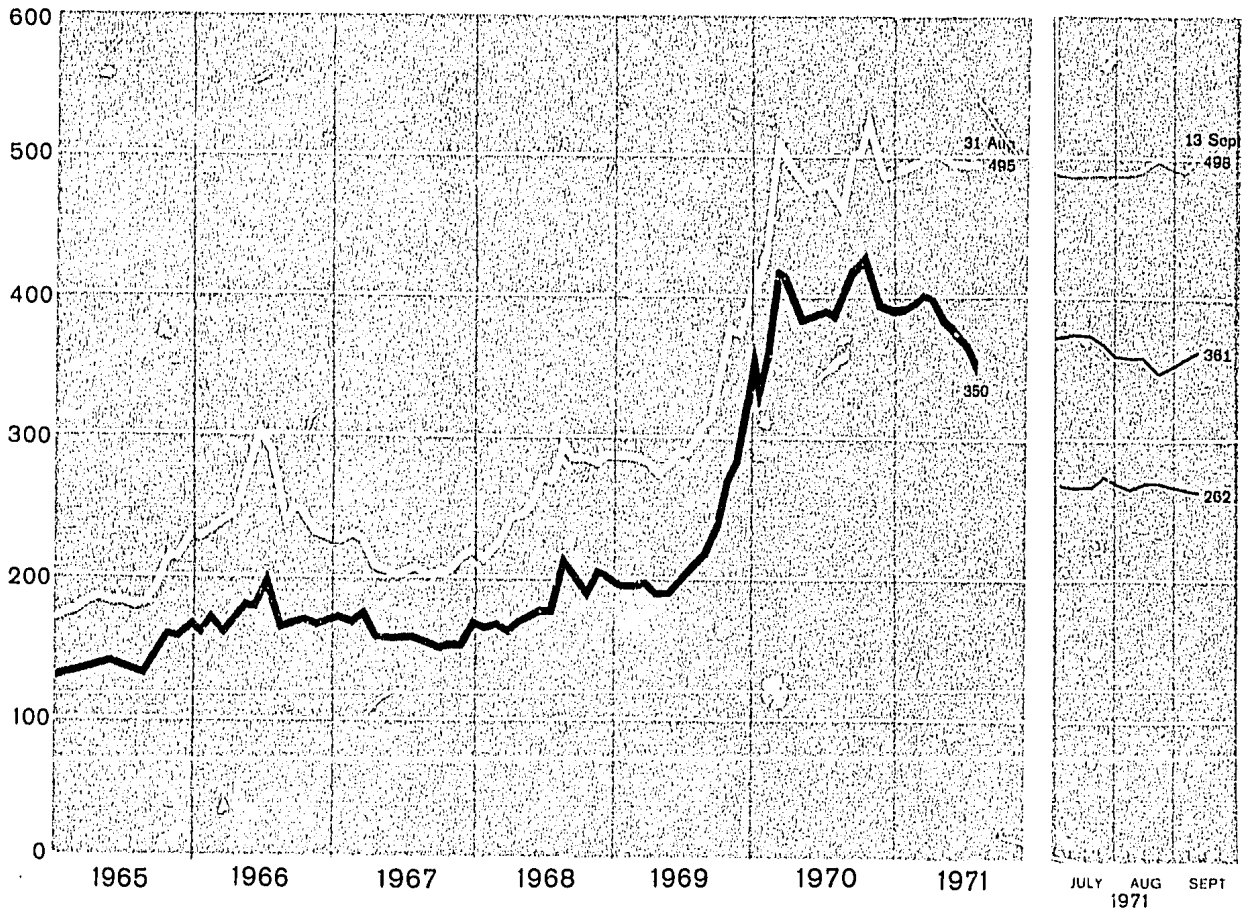


*USAID monthly average retail price index for Saigon

**Data are for end of month

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SAIGON Free Market Gold and Currency Prices Piasters Per US Dollar



GOLD Basis: gold leaf worth
\$35 per troy ounce
— US \$10 GREEN
— US \$10 MPC Military Payment
Certificates (scrip)

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