ECONOMY OF SOUTH VIETNAM

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Historical Background

The separation of South Vietnam from North VietNam in 1954 abolished what had once been an essentially integrated economy with North VietNam the industrialized area, possessing rich mineral resources, and South VietNam as essentially the agricultural area. As a result of hostilities and the separation of the two halves of the once united colonial nation, South VietNam was forced to emphasize to a greater extent industrialization. Steps were taken soon after partition to develop a number of hitherto unexploited natural resources such as the Nang Son coal deposits. Also, to reduce dependence on imports government policy fostered the growth of small scale consumer goods industries.

Prior to WWII the Vietnamese were oriented almost entirely to agriculture as a means of livelihood and to scholarship as a goal of education. It has only been during the past quarter of a century that serious attention was paid to other economic opportunities and to the development of necessary technical and administrative skills. French colonial policy viewed the areas that now constitute North and South VietNam as an economic unit; since the South was considered to be the most productive agricultural area, such industrialization as occurred under French hegemony was concentrated in the northern part of the country.

The remarkable fact about South VietNam is that despite the Indochina war of 1946 to 1954, an almost continual state of civil strife and intensified warfare since 1965, the economy has continued to grow at a fairly rapid rate. Despite the ravages of the French colonial war, economic recovery in South VietNam was rapid after partition; crop production is reported to have increased by 32% from 1955 to 1962, achieving in 1962 record levels. From 1962 to 1965 GNP at constant prices rose by 7.1% per annum according to official statistics. While there was a setback during the years of intensified conflict (1966 to 1969) when GNP rose at a per annum rate of only 1.2%, rapid growth resumed thereafter with an increase of 9.5% in 1969 and an estimated additional increase on the order of 5% in 1970.[1/] Thus it appears that for the 9-year period since 1962 when the official GNP series began in Viet Nam, GNP has increased at an annual compound rate of slightly over 5% a year in aggregate terms and about 2.5% per year in per capita terms: a very favorable record considering the adverse conditions that prevailed.

Natural Resources and Structure of the Economy

In 1970 the Republic of Vietnam (RVN) had a population of about 17.5 million people and a national income of some VN$660 billion. (At an exchange rate of 275:1, this would equal US$2.4 billion, or $137 per capita). Population continues to grow at a rapid 2.6% per annum, and the growth rate of the urban population has been far greater.

1/ Data for 1962 - 1969 from Asian Development Bank, Occasional Papers, No. 4, Dec. 1970, Annex V.B.

It is striking to note that the urban population in 1970 represented about one-third of the total population. In view of economic expansion, goaded in part by inflation and the mobilization of over a million men in the armed forces, a situation of full employment has prevailed for some time. In fact, intensive demand for labor has resulted in a rapid increase of the female portion of the active labor force from about 5% in 1960 to over 30% in 1966. About two-thirds of the active labor force is still employed in agriculture.

VietNam's known mineral resources are limited, but its agricultural resources are great. The Mekong delta is famous as the former rice bowl of Asia. In addition to rice which is the country's principal crop, there has been sizeable production of vegetables, bananas, sweet potatoes, manioc, tobacco and sugar cane, which followed rice in that order of importance in 1969. A wide variety of tropical fruits are grown. Industrial crops include rubber, coffee and tea. Hogs are the most important domestic livestock, followed by chickens and ducks. Marine and fresh fish abound and output in the fishing industry has grown rapidly in the past eight years. The catch of marine fish increased 50% to 445,000 tons in 1970, while the catch for shrimp and crab doubled. The export of fish, which was still significant in 1963, has virtually disappeared presumably because it has been more profitable to sell to the domestic market under the inflationary conditions which prevailed.

The total forest area in VietNam is about 5.6 million hectares and it covers 31% of the national territory. (The total area of South VietNam is 174,200 sq. km or about 67,000 sq. mi.). While there is a great potential for future production from the forests of VietNam, development has been seriously retarded by wartime insecurity and the resultant lack of access to forest areas. The production of roundwood, for example, has only been about half of what it had been in 1941. The development of forest resources will require nationwide surveys and mapping as well as sizeable investments in machinery and equipment.

A picture of the structure of the Vietnamese economy can be obtained from the following statistics, which compare the composition of gross domestic production in 1965 for VietNam and Thailand: 1/

Table A

	Percent	
	VietNam	Thailand
Total	100	100
Agriculture	30.5	32.1
Manufacturing and Mining	11.4	14.6
Construction	1.5	5.3
Electric Power and Water	1.0	0.8
Transportation and Communications	5.0	7.3
Commerce	11.7	18.5
Public Service	24.8	4.6
Other Services	14.1	16.8

A comparison is made with Thailand to show a distribution that is more typically normal for a developing economy. As can be noted from the table, the area of striking contrast is in public services; the war effort in VietNam had raised this factor to near a quarter of the total by 1965 in contrast to 5% for Thailand. On the other hand,

1/ Asia Development Bank, Occasional Papers No. 4, Dec. 1970, Annex V.C. for Thailand. The source for VietNam is Annual Statistics for VietNam, 1970, Office of the President, Table 228, p. 269.

Thailand has been able to devote a far greater share of its resources to the development of industry, commerce and construction.

The other important structural aspect of the economy, the composition of national expenditures by use, can be seen in the following percentage figures for VietNam: 1/

Table B

	1969	1970
Total	100	100
Private Consumption	84.4	80.2
Government Consumption	22.7	21.2
Investments	8.9	7.5
Export (Goods & Services) A/	7.9	9.8
Less Imports	23.9	18.7

A/ Only about a quarter of total export earnings (commodities plus invisibles), in 1970, for example, can be considered normal, since the remainder represent dollar receipts from official US expenditures in VietNam.

The table illustrates how a very high level of government consumption in 1969-70 (consisting in major part of defense expenditures) has been financed by an import surplus which was made possible by foreign economic aid. A decline in the share of imports from 1969 to 1970 was reflected in a decline in the relative shares of consumption and investment.

1/ Ibid and National Bank of VietNam for 1969 and 1970.

Industrial production staged a very strong recovery in 1969 from the adverse conditions prevailing in 1968 in the wake of the Tet offensive and recovery continued at a somewhat more moderate rate in 1970: the production index rose 25% in 1969 and 14% in 1970. The climate for industrial investment in 1970 became more favorable. Approximately 39 industrial enterprises increased the value of their capital assets by VN$2.9 billion during the year about half of which was for capital equipment. The industries which had the greatest increase in investments were food processing, detergents, bricks, ceramics, steel rolling, steel sheet, flour milling, pharmaceuticals and ice production. A few years ago VietNam did not have a plastics industry; today there are more than 75 plastics fabricating and formulating plants producing a variety of consumer goods and intermediate products which formerly had to be imported. While food, beverages and textiles still predominate, even capital goods industries are beginning to appear, as evidenced by steel rolling mills and assembly plants for diesel engines, marine engines and agricultural machinery. One can also see a number of industries emerging that will eventually form a chemical complex. The government is attempting to encourage industrialization by formulating a new investment law that will encourage foreign investors, by establishing industrial parks, and by reorganizing and strengthening the Industrial Development Bank.

Industry broadly defined to include manufacturing, power, and construction now probably accounts for about 15% of GNP. South VietNam has moved from being a country virtually devoid of industry 15 years ago to a status of a moderately high degree of industrialization by the standard of developing countries. The reduction of employment accompanying US troop withdrawals and the gradual future demobilization of the country's armed forces will supply a pool of workers for Vietnamese industry. Likewise, it can be said that continued rapid industrialization will be needed to absorb future accretions of the active labor force.

The most dramatic improvement in the country's economy during the past four years has occurred in agriculture. Prior to the winter of 1966-67 VietNam's price control and import policies favored urban consumers and discriminated against the rural population. Subsequently, this policy was reversed, agricultural product prices were gradually freed to respond to market influences and agricultural inputs were subsidized. The result was to improve farm incomes. Later the introduction of miracle rice seed, increased availabilities of pumps and fertilizers, combined with improved incomes encouraged a rapid expansion in agricultural output. The rice crop harvested at the beginning of 1971 totaled 5.6 million tons, a record crop for VietNam and 30% larger than the one for 1967 when the new program for increased agricultural production was initiated. While from a production viewpoint it appears that VietNam has nearly achieved self-sufficiency in rice, the problem of achieving an effective distribution of rice throughout the country still remains. The Delta surplus must be moved by barge, truck, and coastal vessel to the deficit areas in Saigon and Central VietNam, in amounts approaching a million tons a year.

With self-sufficiency in rice now in sight and with a significant surplus in rice production possibly only a year or two away, the ability of the Vietnamese farmer to produce other crops is of distinct importance. A feed grains production program developed jointly by USAID and GVN agricultural experts in 1967-70 has the aim of increasing the production of corn and sorghum to support the livestock and poultry industries. The number of sows has been increasing at a rate of 20,000 per year, while the egg production capacity of poultry more than doubled during 1970, reaching a rate of 2.5 million eggs. Vegetable production is also increasing rapidly. Other crops such as sugar cane and fruits also have good possibilities of broadening the agricultural base of the economy. If there is to be any significant development of agricultural exports, however, the paramount need is to establish an effective export marketing organization.

Progress in agriculture has not been confined to direct gains in production. A revolutionary new program, known as the Land-To-The-Tiller Law, of March 26, 1970, grants to any farmer who does not own the land he is cultivating, full title, free of charge, if he applies for it. Former owners are paid by the government in cash and government bonds. It is planned that 2.5 million acres of rice land be transferred to actual tillers over a three-year period. It is expected that this new program will do much to dispel in the minds of the rural population the Viet-Cong-inspired image of the rich landlord exploiting the poor peasant.

The discussion of the capabilities and potential of the Vietnamese economy would not be complete without reference to physical and human infrastructure. One of the fortunate byproducts of the presence of large

US military forces in VietNam during the past six years has been the construction of a vast network of roads, bridges, airports, seaports, and communications facilities which, while designed primarily to support a war effort, undoubtedly will be useful in large part to the civilian economy of the future. Employment of the Vietnamese by the US military has resulted in the training of many skilled workers. The government's greatly expanded educational effort, strongly supported by USAID, has resulted in an increase in the number of primary school children from 400,000 in 1954 to 2.2 million in 1970 (84% of the estimated primary school age population). During this same period enrollment in secondary schools increased from 53,000 to 542,000. If hostilities can be ended between North and South VietNam in the near future, it may be assumed that South VietNam can launch a new era of domestic economic development with a stronger physical and human infrastructure than it has ever had before.

Inflation and Stabilization Measures

Serious inflation in VietNam has been a concomitant of the military build up and vast increase in military expenditures between 1965 and 1969. Prior to 1965 the economy was characterized by price stability. Between 1956 and 1964 retail prices as measured by the working class index in Saigon rose by only 14%. From the end of 1964 to the end of 1969 prices measured by this same index rose by 420% while money supply rose 520%. The rapid expansion of the money supply, which led to a parallel although somewhat less steep rise in prices, was primarily a result of the need on the part of the GVN to finance the increase in defense expenditures by borrowing from the National Bank, creating new money for the government to spend.

The increase in government expenditures was largely to pay the wages of a vast increase in military and paramilitary forces. The total of these forces rose from about 500,000 at the end of 1964 to 1,050,000 by late 1969. This large extraction of workers in their most productive years from the labor force contributed to a slow down in economic growth and to inflationary pressures. In addition, the arrival of several hundred thousand foreign troops during 1965 and early 1966 and the construction of air bases and other facilities put added strain on the economy and helped create a gross imbalance between demand and supply. The result was a precipitous rise in prices; from April 1965 to July 1966 retail prices in Saigon rose 125%. Prices rose on the average by 42% per year from the end of 1964 to the end of 1969; even in 1970 retail prices in Saigon rose by 32%, but most of the increase occurred during the first half of the year. A monetary statilization program introduced during the autumn of 1970 brought about a drastic change in the situation. The USAID Retail Price Index for Saigon rose by only 2% during the last quarter of 1970 and from the end of 1970 to July 5, 1971, there was virtually no rise in prices. Price stability was accompanied by a continuous decline in the average monthly piaster price of dollars in the black market (from US$100 = 406 piasters in March to 375 piasters in July), reflecting increased confidence in the local currency.

The stabilization program instituted by the government during the autumn of 1970 and further enlarged during the spring of 1971 consisted of a series of measures to raise exchange rates (partially devalue the piaster) by introducing a 275:1 rate for exports and some imports and invisibles, roughly double interest rates, increase commodity prices by reducing subsidies, raise the perequation tax on imports and establish advance deposits on imports. These measures all had the effect of raising government revenues or private savings and thus to contract the money supply. In June a policy of free licensing of most imports was instituted at an effective exchange rate of VN$400 to the dollar (275 rate plus a 125 perequation tax) and in July interest rates were further raised. It is expected that these measures will have a further contractionary effect on the expansion of the money supply.

From the end of 1970 to June 26, 1971, the money supply rose by VN$20 billion, or by 12%, which would be equivalent to an annual rate of increase of 24%, yet there has been no noticeable rise in prices. During the first half of 1970 the money supply rose by only 6%, yet the retail price level rose by 24%. It is therefore obvious that there is not necessarily any close correspondence between movements in money supply and prices within any short period such as six months. Much depends on people's anticipations concerning exchange rates, future supply of imports, or the political situation. Thus, the improved situation this year may reflect the fact that people have greater confidence in the future or that a more liberal import policy by the government has made people feel more secure about future supply. In a society where 80% of the money supply is held in the form of cash (compared to less than 50% in most developing countries) and where internal security is still uncertain, sudden and sometimes violent changes in expectations can occur which will influence the price level more than the quantity of money.

US military and civilian expenditures in VietNam have been running at a rate of about VN$80 billion a year. Despite troop withdrawals, the rate of such expenditures was roughly stable during 1970 and the first half of 1971. Within a year a very appreciable decline in such expenditures may be anticipated which will serve to reduce inflationary pressure within the economy on the one hand and which on the other will offer the government some scope for increasing public sector investments in its budget. Direct investments in the current budget account for only about VN$13 billion, or 5% of total budget expenditures. One must assume that foreign exchange receipts are not reduced, i.e. that foreign aid will offset any loss in dollar earnings resulting from DOD expenditures in VietNam. If there were no offset to the decline in DOD expenditures, the country could not sustain the minimum level of imports necessary for raising investments and rebuilding the country's export trade.

Problems Associated With Transition to a Peacetime Economy

It now appears that the transition from the wartime economy that has prevailed during the past six years to a peacetime economy will occur in two stages: a) the first stage, of indeterminate duration, will involve the withdrawal of the bulk of the US armed forces placing the full burden of the war on the South Vietnamese armed forces; b) the second stage will occur when hostilities cease as a result of some type of cease fire or armistice which will permit the demobilization of the bulk of South Vietnamese armed forces. Both stages of transition will involve different economic problems than those that have faced the economy in the past. Problems of price inflation will give way to problems of income and employment stabilization, though such problems may be more serious during the second stage of transition. Both stages will require attention to a reordering of priorities in the use of resources, with greater emphasis given to investments for the establishment of import saving or export earning industries, although it is during the second stage that the greatest shift of resources to use for civilian production will be possible. The first stage of transition will involve the loss of the bulk of some $300 million in foreign exchange earnings deriving from US military expenditures in VietNam. While this loss may be largely or entirely offset by greater direct economic aid assistance for some time, there will be a dire need for the country to increase its export earnings to cover the gap.

Troop withdrawals and the accompanying decline of US military expenditures are apt to give rise to serious temporary unemployment in the less developed regions of the economy, such as the northern five provinces, MR-1. The employment problem in this area is intensified by the presence of a large refugee population that generally lacks secure, full time employment, by the low level of industrialization in the region and by what the Joint Development Group termed "the most difficult problem in South Vietnam so far as agricultural development is concerned." This area will require special attention in planning the country's future development.

In 1970 VietNam's commodity exports amounted to $13 million and its imports to $662 million (excluding non-commercial imports), the difference was almost entirely covered by foreign economic aid and DOD expenditures in VietNam. It is obvious that if VietNam is to gain any significant measure of independance of external grant economic assistance, its most important economic goal during the next decade is to raise its export earnings and reduce dependence on imports of commodities that can be efficiently produced within the country. For some time to come economic planning and policy will have to focus on the allocation of resources to meet this objective. It is also obvious that until export earnings have increased manifold, the country will remain, as it is today, heavily dependent on foreign economic aid to support future growth or even to sustain current levels of real income.

The recent adoption of an export exchange rate of VN$350:US$1 is an important step on the long road to achieving a reasonably high level of exports. The highest previous export figure was $85 million achieved in 1960. VietNam must seek over the next decade to achieve a level of exports several times that level. Rice and raw rubber have been the traditional exports of VietNam, but it may be some time before VietNam can become an important exporter of rice again. The world market for rice is soft and may remain so for some time; production of rubber has been hampered by security considerations. A rehabilitation of the rubber industry will require sizeable investments and a number of years before plantations are fully productive. Rubber and other traditional exports, such as duck feathers and cinnamon, face competition from synthetics. Of the traditional exports, only fish offer opportunities for sizeable growth of sales in foreign markets over the long term.

Between 1958 and 1966 VietNam increased its annual fish exports from US$171,000 to US$959,000. Security conditions and lack of manpower due to national mobilization hindered further growth in production and in subsequent years exports virtually ceased as the domestic market absorbed output. Although possessing a large fleet of wooden craft, the fishing vessels are not modern and most of them are not motorized. If VietNam is to enter world markets as a large scale exporter, it will have to make sizeable investments in a modern fishing fleet, cold storage facilities and refrigerated transportation systems.

Forestry, livestock and food processing are the new sectors that offer great potential for export development. Most analysts agree that VietNam's unexploited forests, composed in large part of tropical hardwoods, will require a long period of time to develop since the country has no expertise in the export of timber and wood products. It is an area that may be attractive to foreign investors, since the world consumption of wood and wood products is expanding rapidly. VietNam exports small quantities of vegetable oils and their byproducts, but a recent study indicated that by 1980 VietNam could be exporting vegetable oils at an annual rate of from $6 million to $9 million a year. The country could be an important exporter of animal protein in the form of chickens, swine, buffalo and cattle. In order significantly to develop this potential the country will have to expand greatly its feed-growing industry and establish canning and meatpacking facilities.

External Assistance

Gross economic assistance provided to VietNam by the USA from FY 1964 through FY 1971 amounted to $4,293 million. The AID Program in FY 1971 amounted to $640.1 million. Grant economic and social aid (both official and private) provided by 47 other countries from July 1964 to December 1970 amounted to $146 million, and grant aid provided by international institutions during the same period amounted to $14 million. Since the American troop withdrawal will deprive VietNam of the bulk of the foreign exchange earnings derived from DOD expenditures in Vietnam, even higher annual levels of external economic assistance will be required to compensate for the loss until such time as VietNam's normal export earnings have increased appreciably. As John R. Mossler, Director of the USAID Mission to VietNam, pointed out in a recent speech before the American Chamber of Commerce in Saigon, AID has requested from Congress an Economic Support Fund of $150 million for FY 1972, the dollars being as freely usable as the dollars the GVN has been earning from US military purchases of piasters. If the request is approved, the amount of dollar support for financing imports from all sources should remain stable at about $700 - $750 million.

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