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AMBASSADOR ELLSWORTH BUNKER'S "BACK CHANNEL" REPORT TO
THE WHITE HOUSE - REPORT NO 40 . DATE: Dec. 21, 1970

TELEGRAM

Foreign Service of the
United States of America

OUTGOING AMEMBASSY SAIGON

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REVIEWED BY *McCapra* DATE 4/7/67

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FOR THE PRESIDENT FROM BUNKER

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Herewith my ninetieth message.

1. General. A critical problem with which the GVN has had to contend in recent months, and one of the most difficult to resolve, has been the economic situation. As a result of close collaboration between the GVN and the Mission's economic team, the reforms which I mentioned in my last message were put into effect in early October. The results have been quite remarkable. Prices are only 3 percent above the level of late September, and have headed downward in the last three weeks. Blackmarket currency transactions have been reduced and the market rate for the dollar has declined. Liquidity has been reduced by the large

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| absorption of piasters brought about by advance import | | Date: |
| deposits and new savings and other deposits. As a | | |
| consequence, despite large amounts by the government | | |
| for its wage increase, money supply has not increased | | |

since September. The immediate economic outlook, therefore, appears more favorable than it has been for a long time. There are, however, problems ahead in coping with heavy outlays for government wages, and payments in connection with Land Reform and for veterans' benefits. We are now engaged with the Vietnamese in laying plans for meeting these demands.

2. On the political front, there has been considerable movement. Of greatest importance was Thieu's endorsement of your October peace proposals and his agreement to various steps related to the prisoner of war problem.

Internally, political dynamics are beginning to respond to basic changes in the nature of the conflict and to the prospects

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Classification

Control:

3

Date:

of the national elections in 1971. As of now, Thieu and

Big Minh seem likely to be the major political figures.

Ky is reportedly taking soundings as to his own prospects.

3. Laos and Cambodia have been the scene of increasing military activity and this seems likely to continue in the near future. The enemy is devoting his main effort to re-establishing lines of communication to offset the losses he suffered in the Cambodian operations of last spring and summer. South Vietnamese cross-border operations have

kept the enemy off balance and we have concentrated our air activity to interdict his movements in the Laos Panhandle.

Within South Viet-Nam, military activity continued at a relatively low level, with the enemy maintaining pressure on pacification targets and attempting to build up his political infrastructure. Even with the diminished military activity, enemy losses range between 1,000 and 1,500 killed each week, and ARVN losses between 200 and 300, not counting those killed by

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Control:

4

Date:

assassination and terror.

4. The GVN has succeeded in maintaining momentum in pacification. Elaborate plans have been prepared for a new program with changed emphasis in 1971. The stress will be on consolidating gains and stimulating economic forces and political development, especially self-development. The security situation on the whole benefited from the enemy's distractions in Cambodia, but terrorism and abductions aggravated existing problems in several provinces in MR II.

5. The land reform program is moving into high gear with general public acceptance. Some weaknesses remain to be corrected. The issuance of titles rose to 15,000 in November and the second phase was launched in early December with the first compensation payments to landlords.

6. Economic Reforms Show Early Promise. The economic reform program which was just being put into effect at the time of my last message has been remarkably successful. Supplementing

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Classification

5

Control:

Date:

the high interest rates, liberalization of import financing, and high advance deposits for imports, instituted in September, the main phase of the reform was put into operation on October 5.

It includes:

- a) A new exchange rate of 275 piasters to the dollar (up from 118) for a wide range of transactions, including troop accommodations, exports and luxury imports;
- b) A rise in selected import taxes;
- c) An increase in the price of imported rice in Central Vietnam; and
- d) A wage increase averaging 16 percent for servicemen and government workers.

All of the measures taken together were designed to curb inflation, restore confidence in the piaster, reduce a variety of abuses such as the currency blackmarket, and in a broad sense to start restructuring the economy away from wartime distortions to a more normal, peacetime situation. The

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Control:

6

Date:

program was worked out in coordination with this Mission, and in response to it the United States undertook to provide up to \$750 million in import financing during Fiscal Year 1971, an increase of \$60 million over the volume of import licensing in FY 70.

7. The hard decisions taken earlier have begun to pay off.

Retail prices in Saigon have gone up only 3 percent since just before the reforms were instituted and have recently shown a downward tendency. The average price of imported goods has not gone up at all, despite an average rise of 20 percent in the cost to importers. There has been a sharp reduction in speculation and hoarding. Liquidity has been drastically curtailed and money supply has not increased since September, despite large outlays by the government for its wage increase.

8. The blackmarket rate of the dollar declined from about 430 piasters at the end of September to under 400 at present.

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7

Charge:

Control:

Date:

The volume of blackmarket transactions apparently also has been reduced as evidenced by a higher rate of legal dollar conversions - roughly \$5 million per month after reform compared to \$1.5 million a month before.

9. The only part of the reform that caused popular discontent in one area was the increase applied to the official wholesale price of imported rice in Central Viet-Nam. Inadequate rice stocks and destruction in the fields and warehouses caused by the floods in Central Viet-Nam caused retail prices to rise sharply. The GVN had been committed to make a further increase, countrywide, in the price of imported rice by December 15 in order to establish parity with local rice, but it has now asked for a delay. We are awaiting an explicit GVN plan before taking a position.

10. Other special efforts by the GVN in connection with economic reform deserve mentioning. A large scale nationwide tax census was begun in December by the Ministry of Finance.

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Control:

8

Date:

It is seeking by door-to-door questioning to identify citizens and businesses that have escaped taxes in recent years. Information produced by the survey will be used to collect more taxes and to improve tax administration. It is hoped thereby to reduce and eventually eliminate national subsidies to local government. Firmer measures are also being taken to collect taxes by making heavier initial assessments and auditing suspicious cases. Audit investigations have resulted in increasing tax assessments by more than 200 percent over 1969 and will amount to 1.4 billion piasters in 1970.

11. A second effort, mounted in the customs field with assistance from the U. S. Customs Advisory Team, is aimed at fraudulent declarations. Large scale abuse of the "personal effects" category is being drastically curtailed and there has been a considerable number of confiscations.

12. In the field of economic legislation, the National Assembly

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9

Charge:

Control:

Date:

has passed a new Petroleum Law which will govern oil exploration and exploitation in offshore areas. While the law is vague on some points, we are hopeful the oil companies will be able to work out terms sufficiently attractive that actual drilling will be undertaken soon. A draft of revised legislation covering foreign investment generally in Viet-Nam has also been submitted to the National Assembly and should be enacted during the next several months. A British private consortium is seriously proposing a \$60 million investment in a fertilizer plant.

The three oil companies distributing POL have given informal assurances they will be ready to sign a contract for a refinery in the summer of 1971.

13. The general economic outlook for the immediate future is encouraging. Based on the evidence of price trends, bank deposits, and import licensing, a considerable measure of confidence appears to have been restored. We are entering the

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10

Date: _____

holiday season with an adequate volume of imported goods in the pipeline, and the customary price increases due to pre-Tet demand should be held within normal bounds.

14. The prospect of an excellent rice harvest during the next two months reinforces the generally favorable outlook. The official forecast is for a 1970-71 crop of 5.6 million tons of paddy, an all-time record. This level will bring the country to the margin of self-sufficiency.

15. Looking further ahead, however, we can see problems for 1971. An additional increase in government wages will be necessary, and in view of the September election the GVN may well want this to be a substantial raise. Payments to landlords will be accelerated under the Land-to-the-Tiller program as will payments of higher benefits to disabled war veterans. There may be added election year expenditures of which we are not yet aware. Our current readings of the inflationary gap for

1971, without new counter-measures, shows only a small problem

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Classification
11

Control:

Date:

in the first half of the year, but some potential inflationary problems beginning some time next summer. They should be manageable.

16. It is with these somewhat longer term prospects in view that we have started a joint year-end review with the GVN. A main purpose is to pin down circumstances and criteria under which the GVN should make changes in exchange rates, taxes, and other variables both to keep inflation from re-emerging and to preserve the improvements in structure and state of mind that we sought to introduce in the reform. We are trying to re-establish more normal economic behavior here - to encourage the flow of savings into banks, investment in new production and exports, and bring about a further decline in hoarding and blackmarket activity.

17. Aside from this review with the GVN, we have a series of concerns about the character of our own economic assistance programs. The most basic question revolves around the rate of

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12

Charge:

Control:

Date:

exchange at which the U. S. Government buys plasters for official uses. The rate is still 118 to the dollar, clearly a subsidy rate, and a means by which import financing is made available to the GVN on favorable terms. No doubt this situation must and should be altered soon. The problem is to ensure continuity in the overall assistance level, after the change of rate.

18. In sum, the short term outlook is hopeful, and while there clearly are problems ahead, we are working actively with the Vietnamese to meet them.

19. Thieu Moves on Peace Proposals and Prisoners of War.

President Thieu moved quickly to endorse and give positive support to your peace proposals of October 7. These evoked a remarkably widespread and favorable response in Viet-Nam, similar to the reaction at home and abroad. The feared side effects of a let-down among the soldiers and cadre in the field did not materialize, and observers here agreed that the initiative placed

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Control:

13

Date:

the enemy at a further psychological disadvantage.

20. Recent public attitude surveys show that people see continuation of the war as the dominant national problem, and the peace and war issue will undoubtedly receive special attention in the coming months before elections. Thieu has continued to draw a clear line on coalition and stands on his July 11, 1969 election proposal as a means for the enemy to participate in the political system. This needs to be spelled out, however, in terms that are more specific and more forthcoming. While almost any proposals the GVN might propose would almost surely be rejected by the other side, benefits could accrue to the GVN domestically since it would indicate a determination to continue to work for a peaceful solution and at the same time indicate confidence in its own strength. An important further benefit would be favorable reaction both in the United States and in world opinion which such an initiative would generate. I shall be discussing this with

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Control:

14

Date:

Thieu in the days ahead.

20. After some hesitation, Thieu is also now moving forthrightly on the prisoner of war issue. He gave us notable cooperation on the December 10 exchange proposal and he has his people actively working on another unilateral release of sick and wounded enemy prisoners in the holiday period ahead.

21. Meanwhile, responding to criticisms from inspectors of the International Committee of the Red Cross, the GVN has instituted improvements in the main prisoner of war camp on Phu Quoc Island.

22. Change in Nature of Conflict Increases Strain on Political Structure. Changes in the basic character of the war in Vietnam are becoming clearer as military activity declines to the level of protracted warfare and as our redeployment continues. There is a growing confidence among Vietnamese in their Armed Forces and their ability to meet the military threat.

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15

Control:

Date:

There is also a growing awareness that as the military threat recedes the contest will become increasingly a political one. The enemy is stepping up his efforts on the political front, attempting to penetrate local protest groups to increase divisive pressures and to take advantage of what he calls the contradictions of Vietnamese society.

23. Thieu has laid his plans to cope with the developing political contest. They include step by step economic reform; strengthening and invigorating the administrative apparatus; direct appeal for popular support through local elected officials; acquisition of greater influence in the legislative and judicial branches of the government; and a firm and cautious rein on the military. He counts on a level of American assistance adequate to enable him to carry on the conflict and to enable the economy to move toward more normal circumstances.

24. Other political elements, notably those nationalists who have chosen not to support Thieu, are searching for the means

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Classification
16

Control:

Date:

to assert their influence. The challenges to political
action inherent in the change and the 1971 elections should
constitute incentives for some elements to coalesce. The
main lacking ingredient is leadership and so far they have
not devised a positive program which could present a con-
structive alternative to Thieu's administration. The potential
exists, however, for a strong opposition movement, which
could take advantage of weaknesses in the present administration,
notably its failure to deal vigorously with corruption, to redress
the inequalities of sacrifice, and to cope with economic stresses,
especially in the urban areas.

25. I believe we may also see a rise in expressions of anti-
American sentiment as Viet-Nam begins to stand more squarely
on its feet, and restraints may loosen and pent-up resentments
come to the surface. Close association with us may become a
liability with some segments of public opinion. We are re-
doubling our efforts to reduce frictions in day to day relations

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17

Charge:

Control:

Date:

with the Vietnamese, but I expect we will see deliberate attempts to inflame the issue for partisan, if not for outright subversive purposes, as the Saigon student element has sought to do in recent days over the regrettable incident at Qui Nhon.

26. The challenge of change is beginning to accelerate the internal political dynamics of Viet-Nam. It is in the context of a fundamental transition and with a quickening political pulse that the country is beginning to move toward the crucial test of renewal represented by the national elections of 1971.

27. 1971 Elections Come Into Focus. Although the election is still almost ten months away, the campaign has already begun. Thieu clearly intends to run. General Ducng Van (Big) Minh stated to friends that he also firmly intends to be a candidate. Vice President Ky has not yet made a decision, but is engaged in making contingency plans and taking soundings.

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18

Date:

It is difficult to see how a northerner, such as Ky, could be elected in the present circumstances, although his candidacy could prove a spoiling operation as far as Thieu is concerned.

28. Thieu is expecting to gain support from a fairly wide spectrum of the population - the military, the civil service, elected officials at the village and provincial levels; organized labor; religious elements, Catholics and factions of the Hoa Hao and Cao Dai; ethnic groups, such as the Montagnards, Cambodians and Chinese; and some of the political parties, such as the Farmer-Worker party, the Catholic parties and perhaps some others. His strategy also involves helping a few selected provincial councilmen and some other able men to win election to the Lower House in 1971 in return for help in his election campaign.

29. Other recent steps, including the military and civil service pay raise, ^{and} the promise of a sizeable salary for

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19

Control:

Date:

provincial council members, are also undoubtedly designed in part to increase support for Thieu among these groups. The economic reforms, the Land-to-the-Tiller program, and his relative success in handling dissident elements, such as the students and veterans, should help his cause. Finally, Thieu is carrying his case directly to the people. He now devotes a day or two each week to visiting the provinces and on these occasions he makes a point of explaining his position, mingling with the crowds, and becoming better known in the countryside.

30. Big Minh Presents a Challenge to Thieu. His widespread popularity is expected to draw support from some of the groups on which Thieu is also counting heavily for backing. Minh will probably receive the endorsement of the An Quang Buddhists, despite some indications from An Quang notables of second thoughts about support for the former general. The unresolved issue at this juncture is the extent to which Big Minh can translate

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20

Control:

Date:

popularity which stems from a father image into election organization and votes.

31. Vice President Ky's plans are up in the air at the moment. He would undoubtedly like to challenge Thieu, but his support is limited, and he will probably be able to do nothing more than to split Thieu's vote and throw the advantage to Minh. Unless Ky could strike a deal with Minh which he believed would enable him to control or at least strengthen an otherwise weak Minh government, it seems more likely that he would decide not to become a candidate. The handicap of his northern origin and the fact that the military, as in 1967, would oppose a division in their ranks would tend to confirm this view.

32. A series of recent elections in other branches of the government were conducted with an eye to the major contest in 1971. Pro-Thieu deputies were elected to twenty-two of twenty-five officer posts and standing committee chairmanships in the Lower House.

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SECRET

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21

Control:

Date:

This maneuver was seen as a move to insure greater responsiveness ~~to the executive's~~ to the executive's legislative program, specifically with respect to the drafting of the law which will govern conduct of the 1971 national elections. The internal election of officers in the Senate brought about a clash between the Independents, headed by Senate president Nguyen Van Huyen, and a number of other Senators, mainly those recently elected on the Buddhist slate of Vu Van Mau. The tempest has now passed over, but the victory of the Independents has left some scars and somewhat lessened the prestige of the Senate. Finally, some political significance was attached to the election of Justice Tran Van Linn to be Chairman of the Supreme Court for its current annual term. The Chief Justice is also ex officio chairman of the Central Election Council, which will pass on the qualifications of candidates in the 1971 elections and have a role in considering allegations of irregularities. Linn won

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SECRET

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22

Charge:

Control:

Date:

over former Chief Justice Tran Minh Tiet, who had shown marked independence in a series of important court decisions which went against the executive. Linh is a highly respected jurist and it is generally believed that the Court will function more effectively under his leadership. His election is seen as a victory for Thieu.

33. Battlefield Activity Remains at a Low Level. Overall military activity in Viet-Nam has been light over the past two months. The enemy has avoided large unit contacts when possible and preferred to exert military pressure with attacks by fire and occasional ground attacks. The major single military operation in Viet-Nam was an ARVN attack mounted with division size forces on December 1 in the U Minh forest area of MR IV, a long held enemy stronghold. In contrast to the relative battlefield calm in Viet-Nam, there was an increase in activity across the border in Cambodia and more seems clearly in the offing. The GVN has maintained a force of 12,000.

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23

Control:

Date:

to 15,000 in operations east of the Mekong. A multi-battalion operation, which has just been launched to relieve enemy pressure on the Kompong Cham area on Route 7, was carried out by General Do Cao Tri's forces with great precision.

34. Reduced enemy activity in South Viet-Nam has permitted continued concentration of U. S. air power in Laos, although some air activity continues in support of Cambodia. B-52 Arc Light operations were directed almost entirely against enemy lines of communication in the Laotian Panhandle.

35. Domination of South Viet-Nam remains the enemy's prime goal, but his immediate concern appears to be the need to re-establish his logistical system in Southern Laos and northeastern Cambodia. This has become especially urgent for him since the loss of Sihanoukville and his Cambodian border base areas. At the same time, he is attempting to strengthen the VC political organization and maintain pressure

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SECRET

Charge:

Classification
25

Control:

Date:

"pacification" will be dropped as outdated. The new program will be designated as the Community Defense and Local Development Plan. As the name suggests, it will seek to consolidate territorial security gains by coordinating community defense plans and stimulating local development. The new plan has three overall objectives: Self-Defense, Self-Government, and Self-Development, which explains why the Vietnamese refer to "Vietnamization" as "The Three Selves."

38. Meanwhile pacification has continued to move forward. Effort was stepped up, especially in September and October. The territorial RF and PF were ordered out on operations, especially at night. They were replaced in guard duty on bridges, village offices, and other installations by the People's Self Defense Force. The National Police began the difficult task of taking over the Phoenix program.

39. Despite exhortations from COSVN, enemy activity did not

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SECRET

Charge:

Classification

Control:

26

Date:

disrupt the process. The number of terrorist incidents has gradually declined for seven consecutive months since the peak in April. The November total of civilian terrorism casualties (killed, wounded, and abducted) hit a low for the year and the overall civilian terrorism casualties are now running slightly behind last year's figures despite the higher level of incidents.

40. Mention should be made in this context of the prompt and effective reaction to the recent floods in Central Viet-Nam. Vietnamese led the way with Americans far in the background providing mainly logistics support. Unfortunately, the floods may set back normal refugee operations from three to six months. But the GVN has again demonstrated the ability to organize and carry out a major effort.

41. The "new optimists" in Viet-Nam thus have a basis for optimism. But most of the optimists work either in MR 3 or 4, where the main roads are now open until midnight and where

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Foreign Service of the
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OUTGOING AMEMBASSY SAIGON

SECRET

Charge:

Classification
27

Control:

Date:

the last VC strongholds (Kien Hoa and An Xuyen Provinces) have recently been the scene of successful pacification activity. Some optimists work in MR 1, which is experiencing a 1969-style expansion of pacification despite the late October-early November floods. In MR 2, however, there are some "new pessimists", Vietnamese as well as American. In several provinces there, such as Binh Dinh, Phu Yen, and Tuyen Duc, the VC have mounted campaigns of terrorism and abduction that have had real impact on the population. Such problem programs as Phoenix, People's Information, and Refugees are particularly troublesome in MR 2. The new MR Commander, Major General Dsu, is a great improvement over his predecessor and is working to correct deficiencies, but has many problems ahead.

42. The related all-important question of how many people actually will support the GVN is frequently debated, especially in MRs 1 and 2 where the Central Vietnamese have traditionally

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Charge:

Classification
28

Control:

Date: _____
been dubious of promises from faraway Saigon. The HES shows only what percentage of the population is protected or significantly influenced by the GVN. For questions about support and confidence, the Pacification Attitude Analysis System (PAAS) offers an initial indicator. In it, several trends have been noticeable. A gradually increasing number of people rate the GVN as having "high quality and ability" (up from 44% in January to 61% in November) while a gradually decreasing number of people rate it "low quality and ability" (down from 20% in January to 14% in November). Another trend was that more Vietnamese believe the GVN will win the war (up from 36% in January to 45% in November) while fewer Vietnamese believe that the GVN will not win (down from 32% in January to 22% in November). A former VC in MR 4 recently said, "The people no longer believe the communists will be victorious." Similar reports from the other three regions state that more and more people will not

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SECRET

Charge:

Classification
29

Control:

Date:

cooperate with the VC and want to live in GVN areas.

This could simply be a desire to live in the safest area.

However, these trends suggest less willing support for the VC and perhaps more acceptance of the GVN.

43. Land Reform Gets Underway. The rate at which titles were issued in the Land-to-the Tiller program rose from 5,000 in October to 15,000 in November and Vietnamese officials expect it to reach 30,000 in December and then level off. President Thieu continues to give the program strong support and has personally distributed over 2,000 titles to farmers.

44. Communist propaganda against the law has increased. It appears to have been ineffective and acceptance of the program is good. In a recent survey in MR 4, where 80 percent of the riceland subject to the law is located, almost 90 percent of the people indicated they believe the law benefits the tenant. The same survey showed that in the entire country

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only 8 percent had heard of any attempts by landlords to evict tenants. In some areas, misunderstanding of the rent remission provision needs to be corrected, but on the whole confidence in the government's intent to implement the program fairly is clearly demonstrated in the Delta.

45. Compensation to landlords began in a widely publicized ceremony on December 5 in Go Cong Province (MR 4). The initiation of payments fulfills the last precondition for the release of United States funds through the Commercial Import Program for the support of Land Reform.

46. On November 9, the Prime Minister signed the Montagnard hamlet land decree which provides for defining the boundary of the principal living area of each Montagnard hamlet, including areas of permanent or shifting cultivation. Work on the implementation plan has begun. The importance of this program in the Highlands, where cultivation of

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communal lands has been traditional, rivals that of Land-to-the-Tiller in the Delta in terms of building support and winning allegiance to the government.

47. Conclusion. Among the encouraging recent developments have been:

- a) the increasing competence of the Vietnamese Armed Forces, the excellence of their performance, and their willingness to assume greater responsibility for operations in both South Viet-Nam and Cambodia;
- b) the willingness of the GVN to face up to its economic problems and its courage in taking the action needed to cope with them; and
- c) acceleration of the Land-to-the-Tiller program.

48. Pacification has continued to make progress, although soft spots are still apparent in II Corps. The designation of the program as the Community Defense and Local Development

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Plan is welcome as more descriptive of the program; the term "pacification" is no longer applicable or desirable.

49. It is clear, I think that as the military threat recedes, the content will become increasingly a political one. The need on the part of the government to adopt measures and take action which will unify national elements in its support will become increasingly urgent. This will come into more pronounced focus as preparations for the presidential campaign gain momentum in the post-Tet period of 1971. The effort also to bring some cohesion among the political parties will be an important factor; the ability, or lack of it, to do so in a close election could prove a critical factor in the outcome.

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