

**Table 3. Monetary aggregates evolution <sup>1/</sup>**

Itemization	1996				1997 <sup>2/</sup>			
	Third quarter		Fourth quarter		First quarter		Year	
	R\$ billion	% change in 12 months	R\$ billion	% change in 12 months	R\$ billion <sup>3/</sup>	% change in 12 months	R\$ billion <sup>3/</sup>	% change in 12 months
M1 <sup>4/</sup>	24.3	26.8	29.0	9.2	36.1	54.0	38.5	32.6
Restricted base <sup>4/</sup>	17.2	14.8	20.0	-3.4	25.3	40.2	28.0	39.9
Expanded base <sup>5/ 6/</sup>	165.9	55.7	184.5	50.9	208.2	51.7	239.2	29.6
M4 <sup>5/ 6/</sup>	296.1	28.9	323.0	28.9	352.1	33.6	401.8	24.4

1/ Refers to the final month in the period.

2/ Projected.

3/ Medium point of forecasts.

4/ Working-day balance average in month

5/ End-of-period balances

6/ Preliminary figures for the fourth quarter.

**Table 4. Monetary multiplier <sup>1/</sup>**

Itemization	1996				1997 <sup>2/</sup>			
	Third quarter		Fourth quarter		First quarter		Year	
	Multiplier	% change in 12 months	Multiplier	% change in 12 months	Multiplier	% change in 12 months	Multiplier	% change in 12 months
M1 / Restricted base <sup>3/</sup>	1.408	10.4	1.448	13.0	1.428	9.8	1.373	-5.2
Banking reserves /								
Demand deposits <sup>3/</sup>	0.325	-35.1	0.227	-54.3	0.235	-51.7	0.212	-6.6
Currency / M1 <sup>3/</sup>	0.469	12.5	0.504	18.3	0.516	22.0	0.578	14.7
M4 / Expanded base <sup>4/</sup>	1.800	-16.4	1.750	-14.6	1.691	-11.9	1.680	-4.0

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## Forecasts summary

**Table 1. Observed results and monetary programming forecasts for the fourth quarter of 1996**

Itemization	Forecast		Observed	
	R\$ billion	Percentage change in 12 months <sup>1/</sup>	R\$ billion	Percentage change in 12 months
M1 <sup>2/</sup>	28.6 - 33.6	16.9	29.0	9.2
Restricted base <sup>2/</sup>	20.6 - 24.2	7.8	20.0	-3.4
Expanded base <sup>3/</sup>	159.4 - 187.1	41.6	184.5	50.9
M4 <sup>3/</sup>	289.0 - 339.2	25.3	323.0	28.9

1/ Percentage changes are based on the medium point of forecasts.

2/ Working-day balance average.

3/ End-of-period balances.

**Table 2. Monetary programming for 1997 <sup>1/</sup>**

R\$ billion

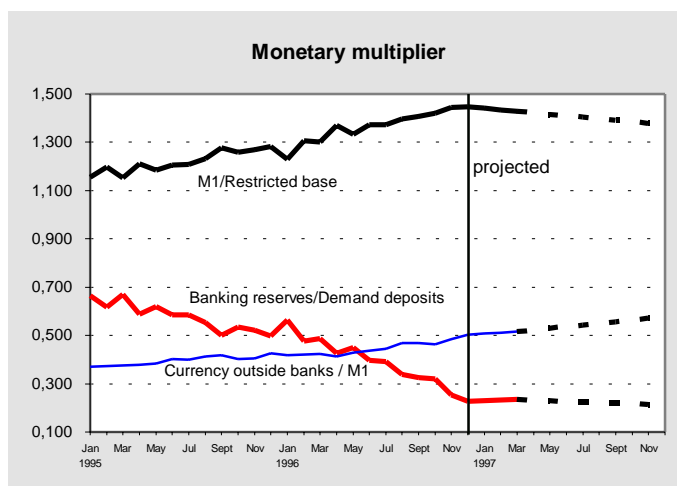
Itemization	First quarter	Year
M1 <sup>2/</sup>	33.2 - 39.0	34.6 - 42.3
Restricted base <sup>2/</sup>	23.3 - 27.3	25.2 - 30.9
Expanded base <sup>3/</sup>	191.5 - 224.8	215.3 - 263.1
M4 <sup>3/</sup>	323.9 - 380.2	361.6 - 441.9

1/ Refers to the final month in the period.

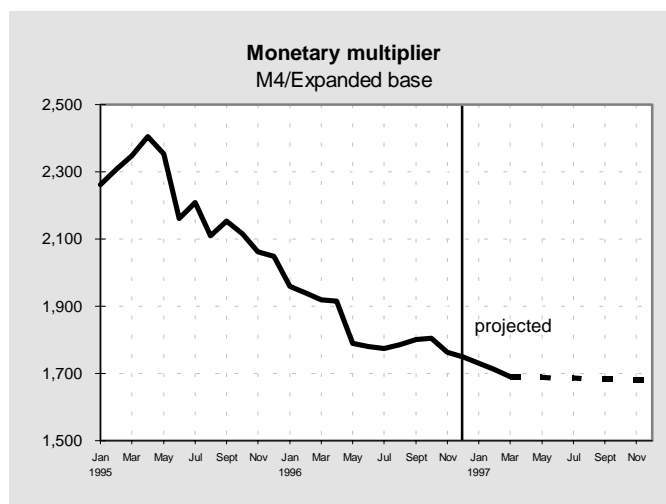
2/ Working-day balance average.

3/ End-of-period balances.

35. Notwithstanding uncertainties about the effects of CPMF on money supply components, it is expected that growth in the ratio of currency outside banks to M1 persist, thus causing a slight drop in the restricted monetary base multiplier.



36. The extended monetary base multiplier is expected to show stability along 1997, thus reflecting the normalization trajectory of private credits.



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Banking reserves / Demand deposits <sup>3/</sup>	0.325	-35.1	0.227	-54.3	0.235	-51.7	0.212	-6.6
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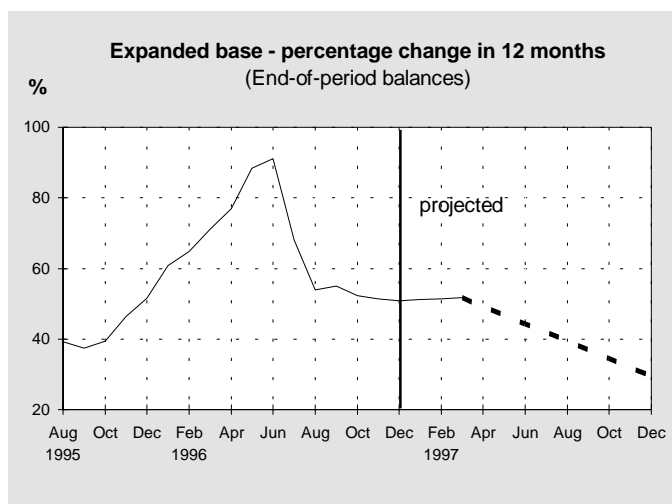
1/ Refers to the final month in the period.

2/ Projected.

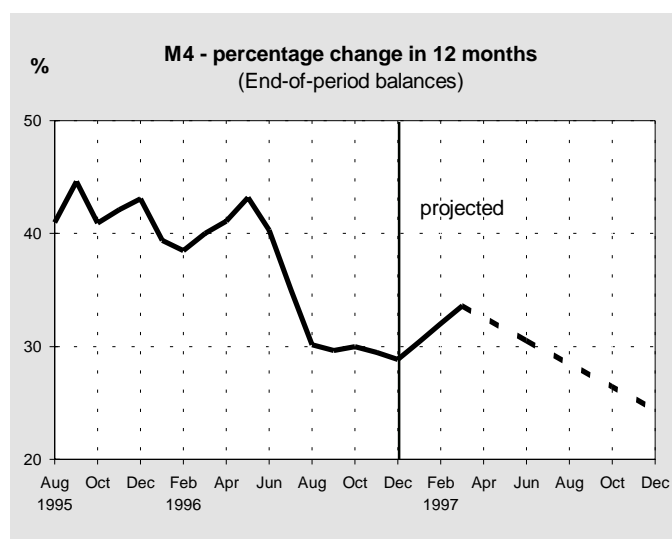
3/ Working-day balance average in month

4/ End-of-period balances.

31. Projections for the expanded monetary base - which take into account expectations of neutral performance of the factors affecting the restricted monetary base - continue to point to a deceleration in the pace of growth, leading to 12-month increases of 51.7% in March and 29.6% in December 1997.



32. In the same way and consistent with the performance pattern of the other aggregates, the 12-month growth for M4 was estimated at rates of 33.6% in March and 24.4% in December 1997.



33. Monetary aggregates e forecasts of values and 12-month variations. Figures for the first quarter and for 1997 are based on the medium point of forecasts.

34. Evolution of the several multipliers, which is implicit in the monetary programming, is summarized in table below:

**Table 2. Monetary programming for 1997 <sup>1/</sup>**

R\$ billion

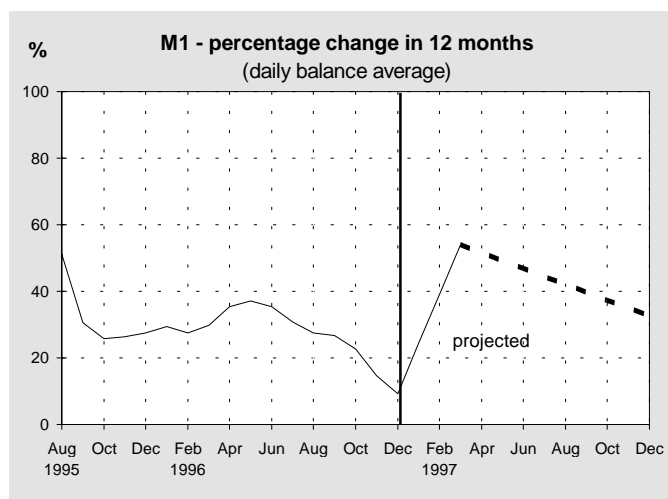
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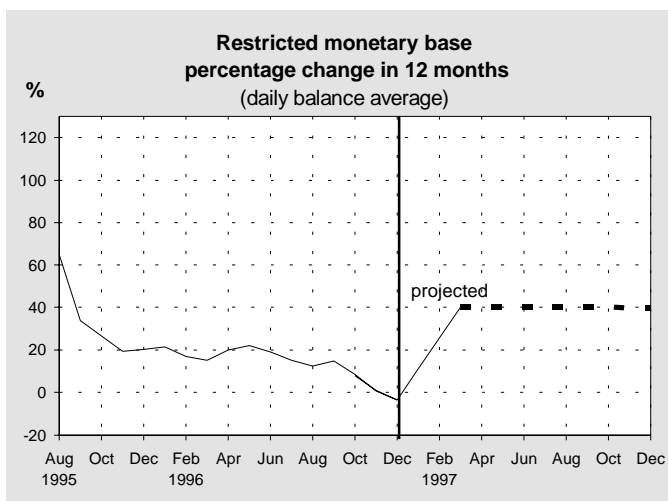
2/ Working-day balance average.

3/ End-of-period balances.

29. The collection of CPMF – which should start on 1.23.97 – should reduce investments in short-term funds, thus making it possible that projection for the 12-month change of monthly average of M1 (currency outside banks plus demand deposits) show increases of 54.0% in March and 32.6% in December 1997.



30. Based on the foreseen performance of demand for currency (M1) and on the expected trajectory of the monetary multiplier – which points to an upward trend in the ratio of currency outside banks to M1 and to stability in reserve requirements -, it was possible to forecast 12-month increases of 40.2% in March and 39.9% in December 1997 for the monetary base (currency issued plus banking reserves).



Financial Transaction (CPMF). On the side of expenditures reduction, one should emphasize layoffs of civil servants with no job stability, extinction of functional ascension to the upper class at the time of the employee's retirement, restriction on the system of benefits derived from occasional substitution and prohibition of payment for overtime. Additionally, it is expected that about one thousand job positions in the direct administration, whose duties are considered unnecessary or liable to outsourcing, be extinct.

25. Within the framework of the privatization program, budgetary proposal for 1997 sets that all the earnings derived from the privatization program, in the federal scope, be destined to the amortization of public debt. It should also be stressed the incentive intended to be given to the program in terms of its extent and speed, including increase in sales of state government companies and in the grant of public services.

26. Recovery of state finance depends on the stimulus given by the agreement on debt restructuring settled by states and federal government, at more advantageous conditions of terms and interest rates, followed by effective commitments regarding public expenditure reduction and privatization of state companies.

27. Balance of payments' result in 1997 is expected to show more equilibrium, thus permitting a certain stability in the level of international reserves. Exports are supposed to react favorably in front of the measures adopted and the process of restructuring and modernization of the Brazilian economy, given the more competitive environment generated by an open economy. Additionally, increased amounts of longer term foreign capital are expected to enter the country, mainly in the form of direct investments.

#### **D - Indicative targets of monetary aggregates evolution.**

28. Programming of monetary aggregates for the first quarter 1997 and estimates of indicators for the year end took into account the expected performance of inflation rates, GDP, interest rates, foreign sector, National Treasury and liquidity assistance to the financial system. Institution of charge on financial transactions – represented by the CPMF – raised the uncertainty about the expected behavior of economic agents, thus representing additional obstacle to the projection of the more liquid aggregates. Table above presents the bands projected for monetary aggregates for the late first quarter of 1997 and for the entire year.

19. The year of 1996 witnessed improvements in monetary policy instruments. The rediscount mechanism was enhanced and the market turned to take a more active part in the settlement of interest rates. It was created the TBC - Banco Central Basic Rate - and the TBAN - Banco Central Assistance Rate -, which determine the cost of rediscount for financial institutions. These rates are settled in function of the guaranties that are offered and the frequency with which financial institutions ask for financial assistance on the part of the Monetary Authority.

### **C - Outlook for the first quarter of 1997 and for the year as a whole**

20. The monetary policy orientation is based on the continuity of the more flexible trend of gradual reduction in interest rates adopted in 1996. This posture should assure the level of credit necessary for the economy to grow in the next quarter, period along which economic activity is traditionally stimulated by the agricultural sector.

21. The outlook for the year points to economic growth at a rate higher than that registered in 1996, given the expected trajectory of decreasing interest rates.

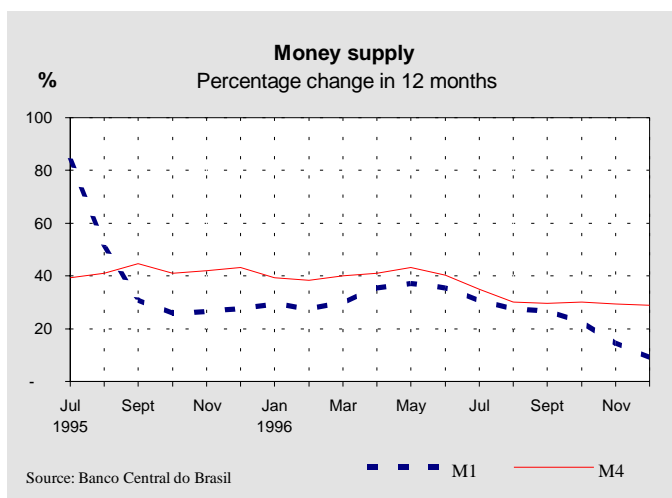
22. Inflation rate in 1997 is expected to stay between 6% and 7%, thus confirming the consolidation of the economy's deindexation process. It is expected that price indices will show the same performance in the first quarter as that they did in the final months of 1996, with growth rates of about 0.5% per month and occasional changes explained by the occurrence of seasonal factors.

23. Expectations of public accounts performance in 1997 are favorable. Besides the approval of constitutional changes regarding administrative, social security and fiscal reforms, the government counts on favorable results from infraconstitutional measures adopted in late 1996, with the aim of improving the process of reducing the fiscal imbalance of public sector. The target for 1997 consists of a primary surplus of 1.5% of GDP, of which 1% on the part of the central government, 0.5% on the part of state companies and balanced accounts of states and municipalities.

24. Besides the expected increase in tax collection due to higher economic growth, revenues should also increase in function of measures that have been adopted, such as change in tax legislation, change in the basis for calculating the Social Contribution on the Net Profits and creation of the Provisional Contribution on

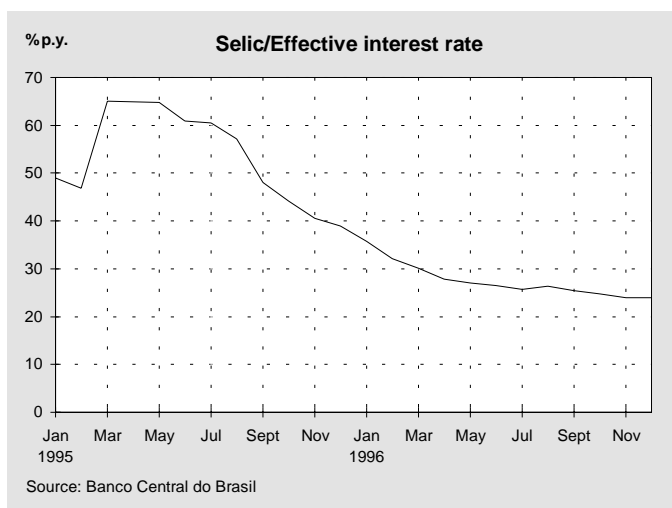


16. The M1 daily balance average came to R\$ 29 billion in the month of December. This amount is within the interval estimated in the monetary programming for the fourth quarter (R\$ 28.6 billion - R\$ 33.6 billion), for growth of 19.2% in relation to the month of November resulted from the seasonal increase in demand for currency due to Christmas period. In 1996, this monetary aggregate expanded by 9.2%.



17. The M4 - the broader liquidity concept in the economy - reached R\$ 323 billion at the end of December, for respective growths of 28.9% and 3.2% in year and in month. As well as the other aggregates, the M4 remained within the interval estimated in the monetary programming for the fourth quarter (R\$ 289.0 billion - R\$ 339.2 billion).

18. The process of gradual reduction in interest rates in the Brazilian economy was maintained in 1996. The outlook for the fiscal area avoided more accentuated drops. Along the fourth quarter, the continuity of this policy was well mirrored in the performance of the effective Selic rate, which moved from 24.75% per year in October to 23.87% per year at the end of 1996, while in December 1995 it was at a level of 38.96% per year.



13. Foreign exchange operations in the free rate market showed net inflow of US\$ 7.5 billion in the fourth quarter of 1996. Trade operations registered deficit of US\$ 340 million, while financial transactions presented surplus of US\$ 7.8 billion. It deserves mention the significant inflows in the form of direct investments and financial loans.

## **B - Monetary programming in the fourth quarter of 1996**

14. The restricted monetary base, in terms of average daily balances, totaled R\$ 20.0 billion in December, or slightly lesser than the lower limit of the monetary programming for the fourth quarter of 1996, in which values were estimated within the interval between R\$ 20.6 billion and R\$ 24.2 billion. The amount of this monetary aggregate in December declined by 3.4% in relation to that in the correspondent month of the previous year and grew by 18.9% in comparison to that of last November. Among the components of the monetary base, banking reserves showed a 57.0% decline in the 12 month period ended in December, while money supply evolved by 27.6%.

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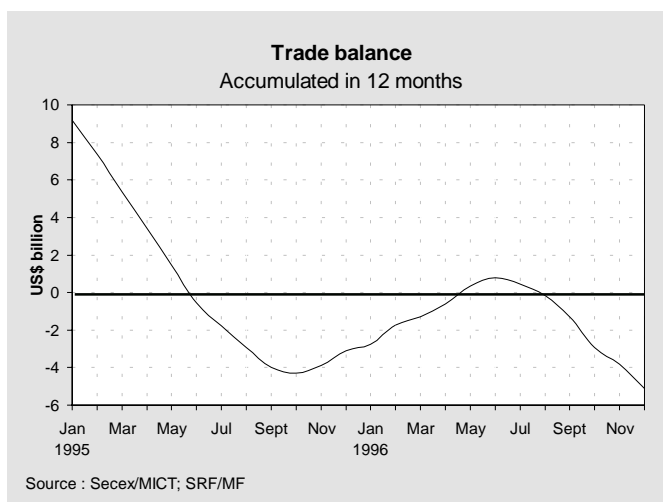
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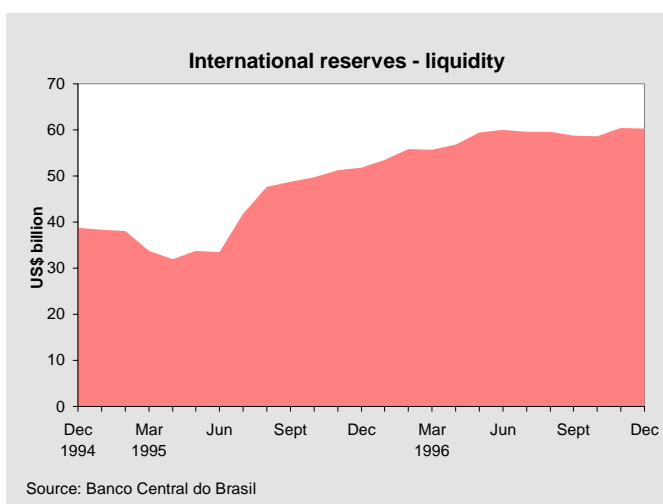
15. The expanded monetary base – composed of the restricted monetary base plus federal securities and the rest of reserve requirements in cash – came to R\$ 184.5 billion in December, thus remaining within the interval estimated in the monetary programming (R\$ 159.4 billion - R\$ 187.1 billion) and showing increases of 11.4% in the fourth quarter and 50.9% in relation to December 1995.

10. The trade balance showed an estimated deficit of US\$ 5 billion in 1996, with imports growing at a pace faster than that of exports – 6.4% (estimate) as against 2.7%. Economic activity growth, mainly in the second half of the year, was responsible for the increased deficit in the year – besides the greater demand for imported goods, part of external market-oriented production was shifted to the domestic market. The joint participation of capital goods and inputs (including fuels) in total imports – considering the first 11 months – evolved from 78% in 1995 to 82% in 1996.

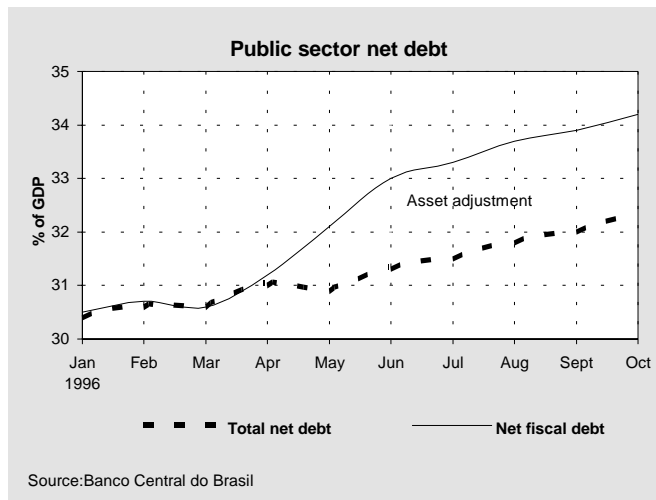


11. In 1996, the estimated ratio of current transaction deficit to GDP reached 3.1%, which is higher than that of 2.5% registered at the end of 1995. However, the profile of the deficit financing improved significantly, deserving mention the increased relative participation of medium- and long-term loans and particularly of direct investments, whose net inflows increased from US\$ 3.9 billion in 1995 to US\$ 9.4 billion in 1996.

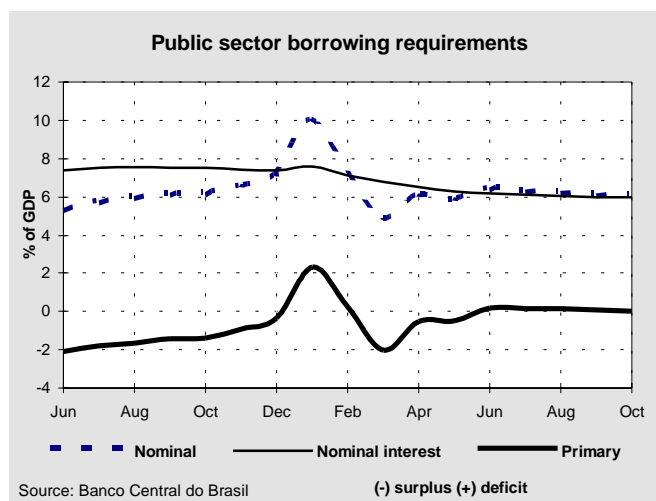
12. As a consequence of this increase in total inflow of capital, international reserves grew by US\$ 8.3 billion, making it possible to reach a balance of US\$ 60.1 billion in the concept of international liquidity, at the end of 1996. Gains in reserves in the final quarter of the year amounted to US\$ 1.3 billion, after having registered stability along the third quarter.



7. Public sector net debt totaled R\$ 260.3 billion in October 1996, or 34.2% of GDP, as compared to 29.9% in the late 1995. Part of this growth (1.9% of GDP) was due to capitalization of the Banco do Brasil and to acknowledgment of debts of previous years. Excluding these net debt asset adjustments of, one can get the net fiscal debt, which totaled R\$ 245.9 billion in October, or 32.3% of GDP. Nevertheless, as from July, growth in total debt showed a certain stability, with net domestic debt coming to R\$ 227.3 billion in October, while net foreign debt amounted to R\$ 33.0 billion.

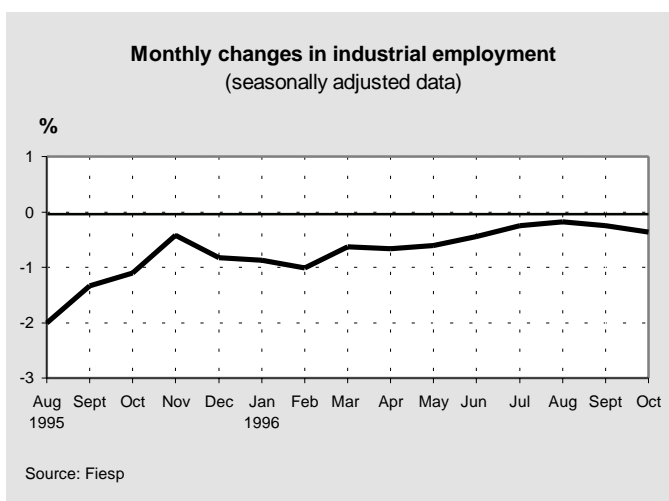


8. Public sector borrowing requirements (PSBR) accumulated a primary deficit up to October equivalent to 0.02% of GDP up to October, as against 0.06% up to September. This unfavorable result relatively to the same period of 1995 - which registered a surplus of 1.4% of GDP -, derived from lower surplus of the central government and the Banco Central, which moved from 1.32% of GDP in 1995 to 0.48% in 1996, and higher deficit of states and municipalities, which increased from 0.13% to 0.81% of GDP, respectively, while surplus of state companies climbed from 0.21% to 0.31% of GDP.

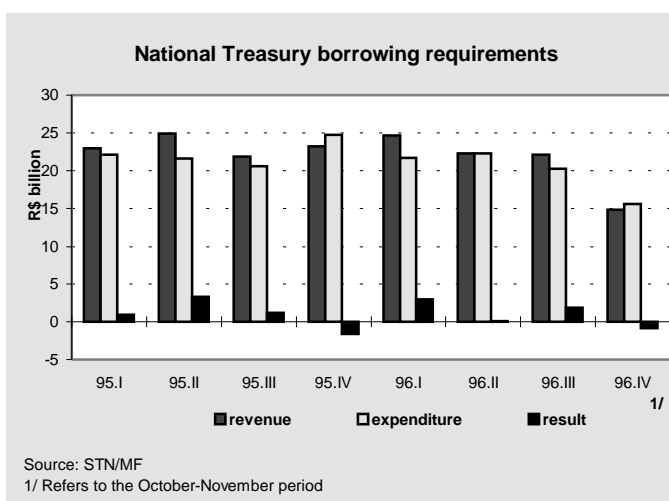


9. Inflow of resources in the scope of federal privatization amounted to US\$ 4.1 billion in 1996. The most significant participation corresponded to electrical energy and railroad sectors, which accounted for 58% and 36%, respectively, of these revenues. State privatization programs started in 1996, generating a revenue of US\$ 1.3 billion.

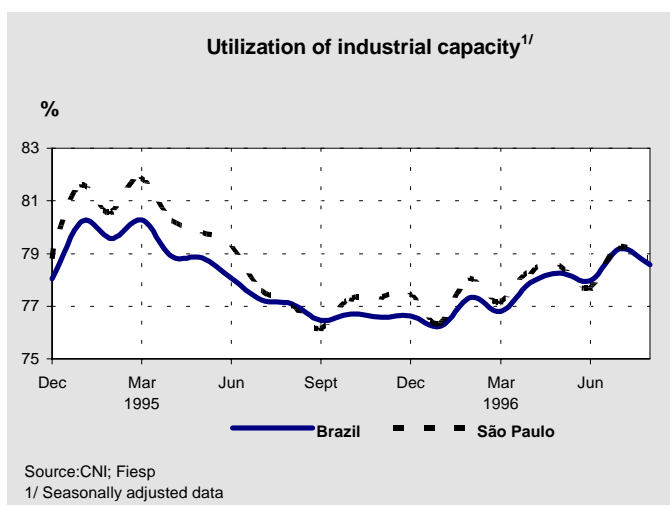
5. The level of employment indicator elaborated by the Ministry of Labor showed growth of 0.2% up to October, mainly because the positive evolution of job positions in building industry and in services. Insofar as industrial employment in the state of São Paulo is concerned, drop was less intense in those months in which the economic activity showed better results. It was particularly true in the third quarter, period in which the Fiesp indicator was more stable. Evolution of employment in São Paulo industry also reflects the process of industrial decentralization carried out in recent years.



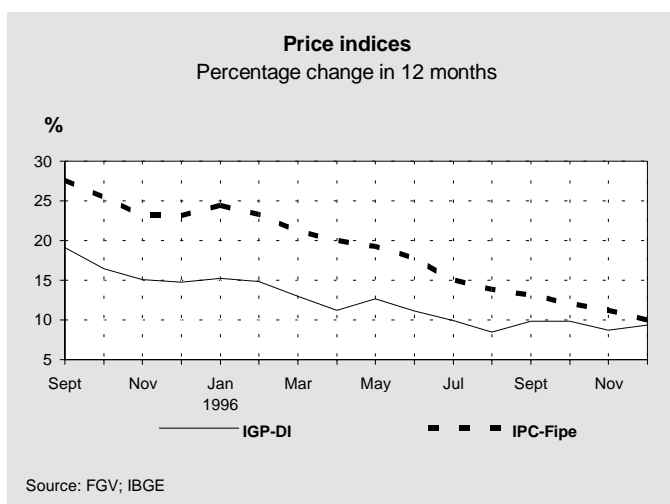
6. In the October-November period, National Treasury budget operations, in the concept of borrowing requirements, showed a primary deficit of R\$ 826 million, due mainly to increased outlays under “other current expenditures and investments”. The January-November period accumulated a surplus of R\$ 4.0 billion, equivalent to 0.57% of GDP (0.93% in the same 1995 period). Revenues came to R\$ 84 billion, for a drop of 1.1% in relation to the same 1995 period, while expenditures totaled R\$ 80 billion, for growth of 1.8%. Despite the worse fiscal performance relatively to 1995, National Treasury operational deficit came to 1.11% of GDP, or close to that of 1.01% in the same period of the previous year. This was a consequence of reduction (accrual basis) in real interest outlays, which registered drop of 11.4%. National Treasury cash performance, in its turn, showed a R\$ 2.5 billion deficit in the two-month period - due to concentration of external debt interest outlays in October - thus accumulating a negative result of R\$ 7.8 billion up to November, of which, R\$ 2.2 billion correspond to the item “amount to be paid”.



3. Utilization of industrial capacity along the second half of the year (79%) was clearly higher than that of the first half, although not meeting the levels registered in late 1994 and early 1995. Despite the maintenance of industrial growth pace at high levels in last months, there have not been occurred problems in relation to domestic supply or price levels.



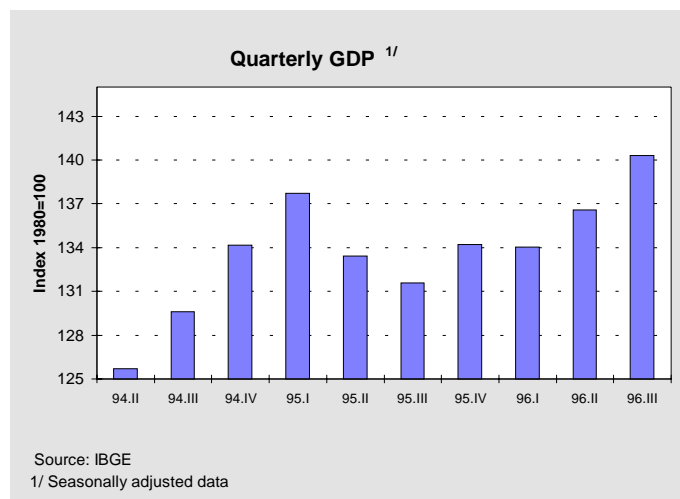
4. Consumer price indices continued to present a slowdown trajectory in the final quarter of 1996, accentuating their convergence to general price indices. This fact reflects a relative symmetry of prices of tradable and nontradable goods. Growth in 12 months of consumer price index - Fipe (IPC-Fipe) and general price index - domestic supply (IGP-DI) - which registered rates of 24.4% and 15.3% respectively in January 1996, declined along the year, coming to 10.0% and 9.3% in December. It should be emphasized that, even when economic activity increased during the year of 1996, inflation remained under control. Growth in price indices registered in certain months derived, for the most part, from public tariffs readjustments.



## Monetary programming for the first quarter of 1997

### A - The economic scene in the fourth quarter and in 1996

1. In the third quarter of 1996, Brazilian GDP registered growth of 2.73% in relation to the immediately previous quarter, in the seasonally adjusted series. This has been the most significant performance since the early 1995. The strongest expansion was registered under farming and livestock (5.64%), principally crops (9.14%). Industry also presented a significant increase (3.65%), seeing that expansion under manufacturing industry came to 4.23%.



2. Based on IBGE data, industrial production showed a drop of 0.17% in October as against the previous month. After having registered a 4.3% growth in July, the seasonally adjusted series has been maintained at the same level. Indicators of the level of activity point to an improvement in November 1996: growth in industrial production is expected to have reached 2.5% in that month.

