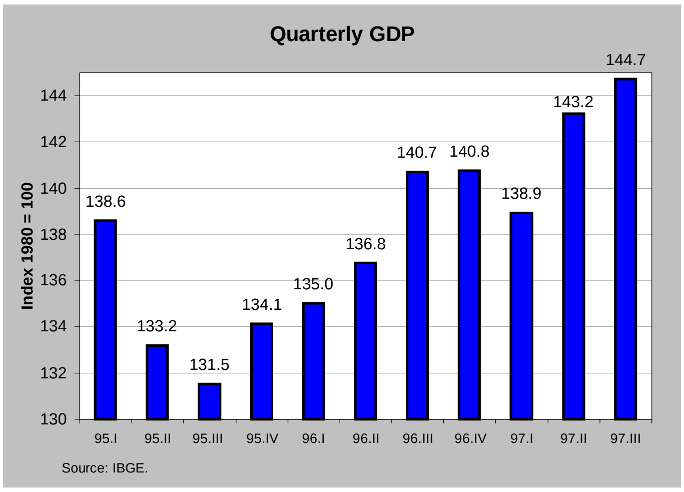
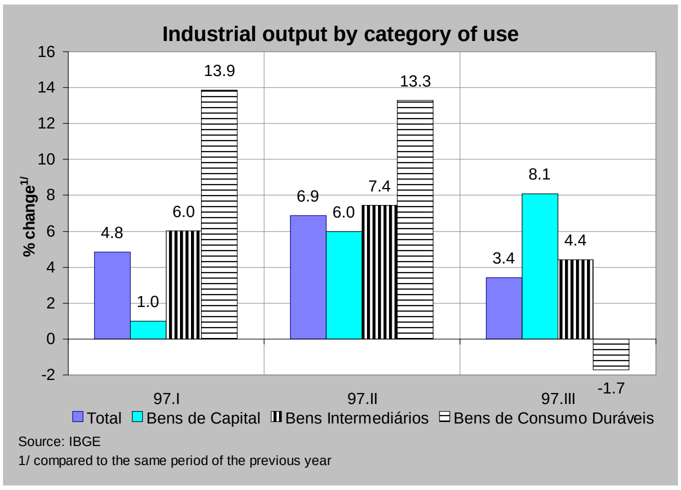
Monetary program for the first quarter of 1998

A. The economy in the fourth quarter of 1997

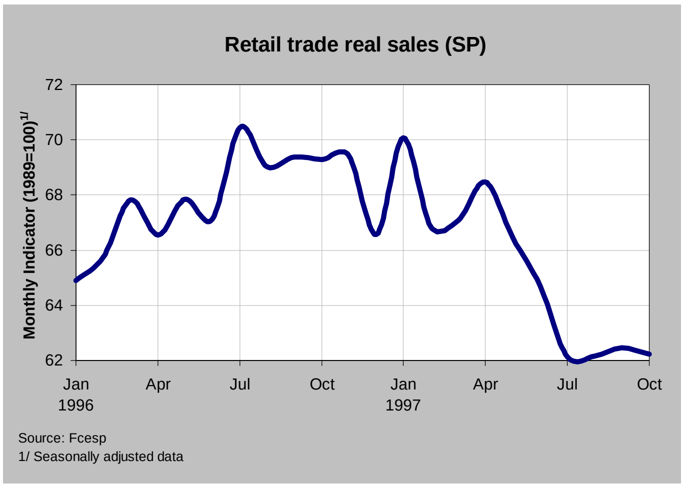
1. In the seasonally adjusted series, gross domestic product (GDP) expanded by 1.1% in the third quarter of 1997, when compared to the immediately previous quarter, when growth came to 3.1%. For the most part, this reduction in the growth pace reflected a more even industrial production trajectory following the high level of second quarter expansion. In terms of the average for the last four quarters, GDP growth came to 3.9% and was led by the industrial sector, particularly the subsectors of mineral extraction and construction.



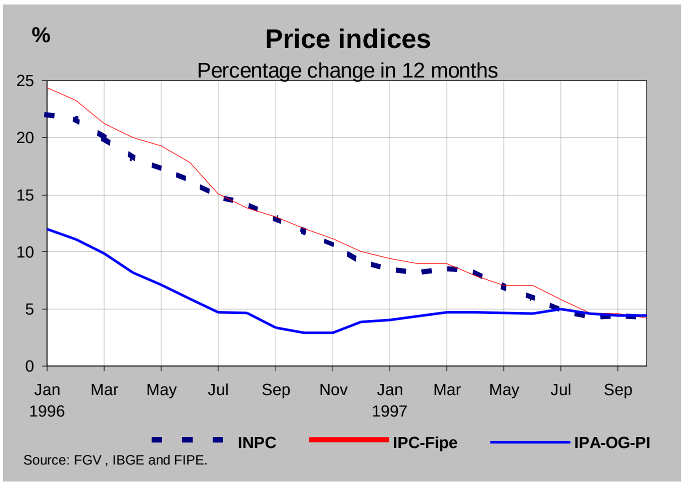
2. In the third quarter of the year, deceleration of the industrial sector was accompanied by changes in composition. For example, durable consumer goods production — previously the strongest segment – closed with a decline of 1.7% when compared to the same quarter of the previous year. The segment of capital goods expanded by 8.1%, though it was precisely this item that had registered the lowest rates in the first two quarters of the year. In the month of October, industrial production increased by 0.43%, according to data purged of seasonal factors. The highest growth was registered under capital goods production.



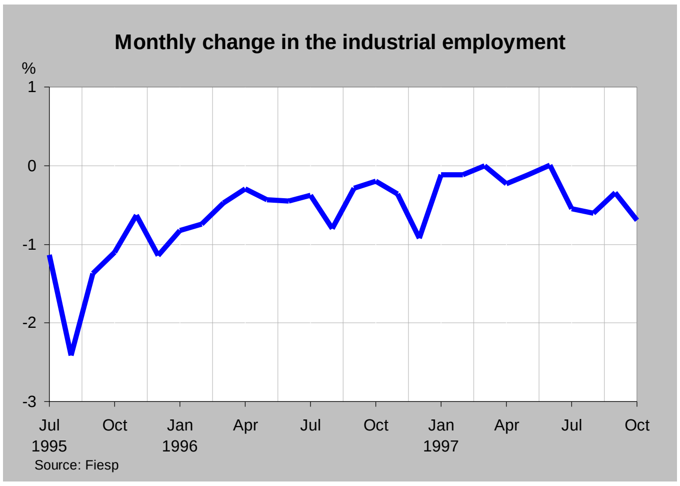
3. According to Fcesp, real billings of the retail trade sector in the metropolitan region of São Paulo turned in a reduction of 0.4% in the month of October, based on the seasonally adjusted series. With this result, this variable has been practically stable over the past four months. The fact that this indicator stabilized at a relatively low level has contributed to the drop in consumer goods production. In accumulated terms for the year, billings registered a drop of 4.3%, with declines under the segments of consumer goods and building materials and an increase in the automotive sector.



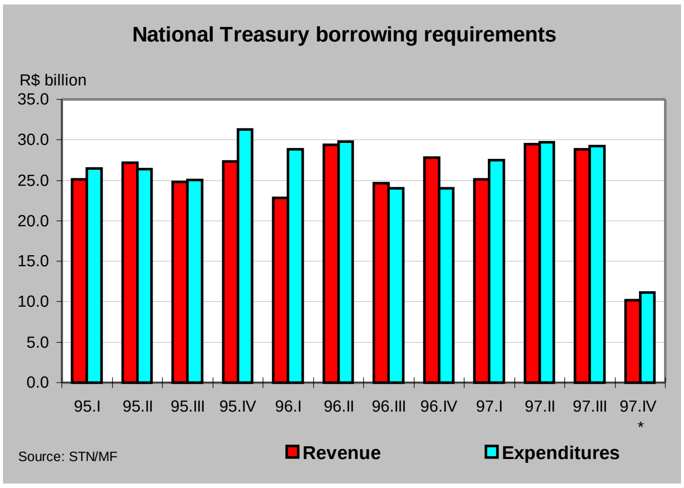
4. In 1997, the growth pace of the different consumer price indices slowed steadily. In 12 month terms, the INPC and IPC-Fipe accumulated rates of 4.3% and 4.2% up to October, as compared to 9.1% and 10% to the end of 1996. With respect to wholesale industrial prices, the IPA-OG for industrial products – a stand-in for growth in prices of tradables – moved from 3.9% in 1996 to 4.4% in accumulated terms in the 12 month period ended in October. Thus, one could observe an evident process of convergence in the price growth rates of tradables and nontradables which, coupled with exchange devaluation higher than the aforementioned rates, aided in enhancing the foreign competitiveness of the economy without in any way compromising price stability.



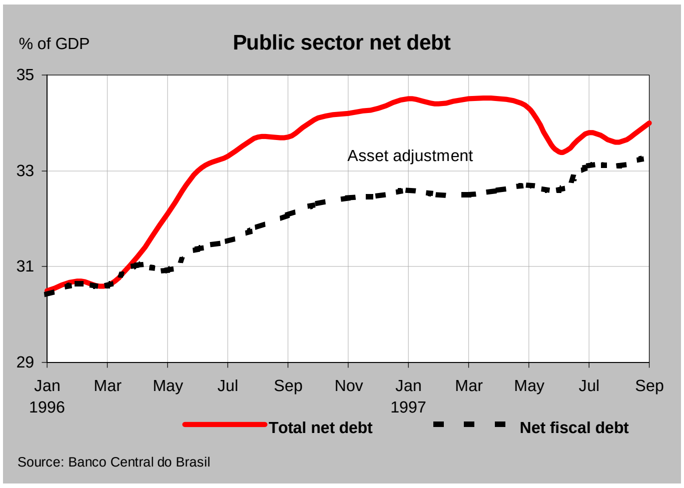
5. The process of restructuring productive activity, particularly in the industrial sector, impacted the labor market during all of 1997. By way of example, in October, the employment level of São Paulo industry closed 2.7% below the December 1996 mark. Ministry of Labor data on formal employment, including all the different sectors and regions, indicated a rise of 1% in jobs up to August, with particularly strong growth under construction (2.7%) and commerce (1.4%).



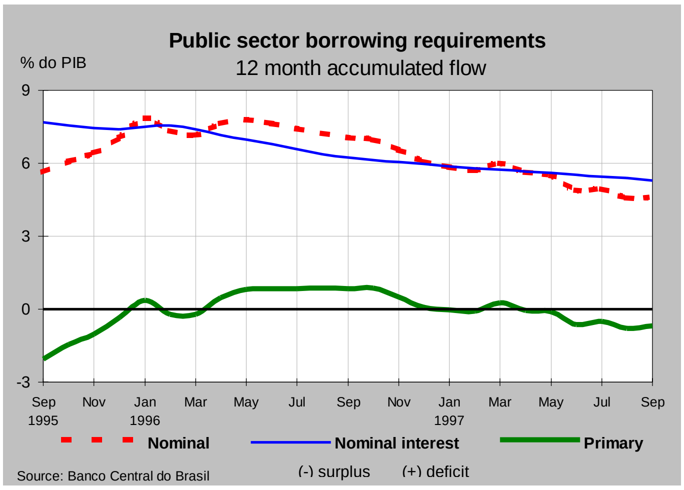
6. In the month of October, National Treasury budget operations registered revenues of R$ 10.2 billion and expenditures of R$ 11.1 billion. In the year, accumulated revenues totaled R$ 93.6 billion (13.4% of GDP) and expenditures came to R$ 97.6 billion (14% of GDP), for real growth of 10.3% and 6.6%, in relation to the same period of the previous year.



7. The net public sector debt (DLSP) came to a September balance of R$ 286.8 billion, equivalent to 34% of GDP. The net fiscal debt totaled R$ 280.4 billion, or 33.3% of GDP. In its turn, the asset adjustment has been maintained in the range of 0.8% of GDP in recent months. This adjustment represents changes in DLSP that are not classified as fiscal results, such as incorporation of the results of privatization operations and of the accounting of contingent liabilities.

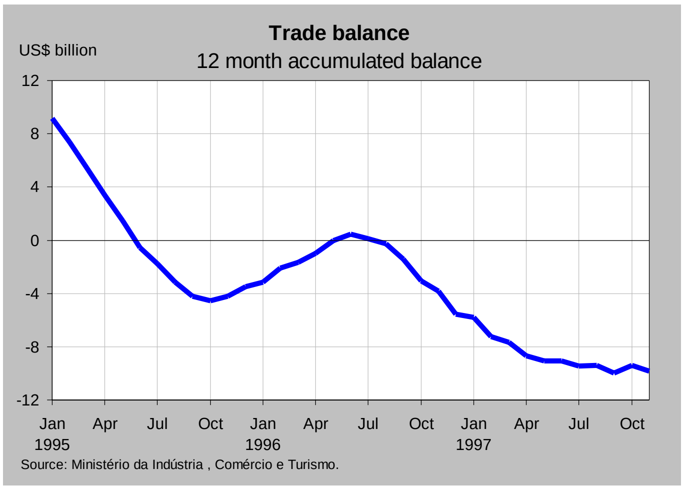


8. When one considers accumulated 12 month flows, public sector borrowing requirements (NFSP) have tended downward during the year, reaching September levels of 4.6% of GDP in the nominal concept and 2.7% of GDP in the operational concept. This trajectory is due to improvement in the primary result of the states and municipalities and state companies and to reductions in interest due by the central government.

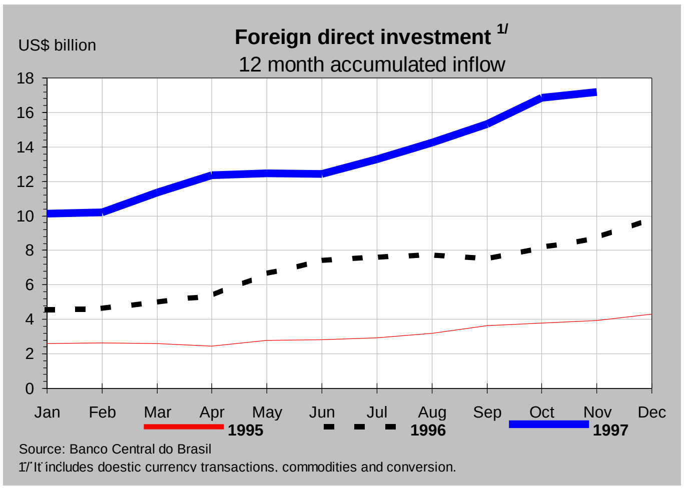


9. In light of the uncertainties that marked the international scenario in the first half of November, the government announced a series of measures aimed at improving fiscal performance, balance of payments results and the competitiveness of national companies. Among these measures, the most important were as follows: cutbacks in expenditures programmed for 1998, channeling of financial surpluses generated by state company funds and dividends into amortization of the public debt, increases in tax collections resulting from higher industrialized products tax rates on cars and beverages, increases in the individual income tax and income tax on fixed yield funds, creation of Advances on Exchange Contracts (ACC) for "indirect exports" for purposes of financing production of inputs for exported goods, expansion of the National Privatization Program, growth in the prices of petroleum derivatives, reprogramming of investments and state company debt limits, reductions in ceilings on credits granted to the public sector by the banking system based on anticipated budget revenues (ARO) and long-term debt.

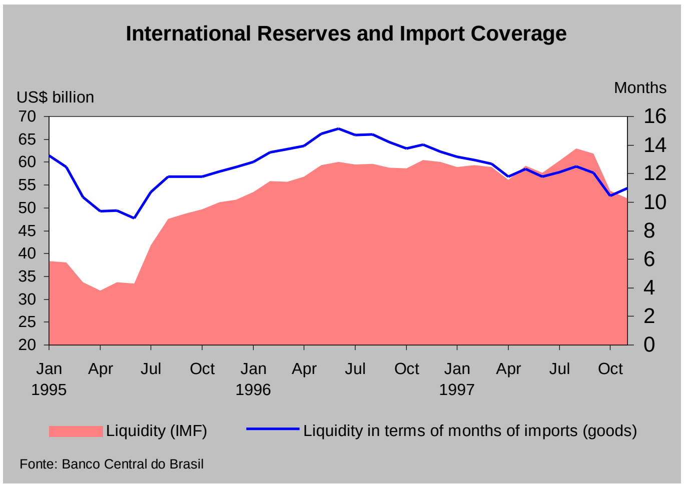
10. In the October-November period, exports came to US$ 8.8 billion, for growth of 8.2% in relation to the same period of the previous year, while imports reached a level of US$ 10.9 billion or 5.8% more than in the same period. The trade balance turned in a deficit of US$ 2.1 billion in the same period. An analysis of trade balance performance in the January-November period shows that exports added up to US$ 48.5 billion and imports came to US$ 56.6 billion, or 10.2% and 18.7% more than in the same 1996 period. The accumulated deficit for the period came to US$ 8.2 billion.



11. The first three quarters of the year closed with a negative current account result of US$ 22.6 billion. When one includes the October-November deficit of US$ 7.2 billion, the first eleven months of the year closed with a negative result of US$ 29.8 billion (4.2% of GDP). The current account deficit in the 12 month period up to November came to US$ 34.4 billion (4.4% of GDP). The net flow of direct foreign investment financed 49.9% of this result. These investments came to a total of US$ 17.2 billion in the first ten months of the year. Foreign investments in the capital market reached a net total of US$ 5.4 billion. In the same period, the gross inflow of foreign financial loans totaled US$ 31.1 billion.



12. International reserves remained relatively stable in the first half of the year before increasing sharply in the third quarter. However, intensification of the Southeast Asia crisis in October led Banco Central to adopt a seller position on exchange markets in order to meet market demand. The obvious results were consecutive drops in the reserve level of about US$ 8.3 billion in October and US$ 1.7 billion in November. Consequently, at the end of November, international reserves totaled US$ 52 billion in the international liquidity concept, corresponding to 11 months of imports.



13. Exchange contracting operations in the free rate exchange market registered net inflows of US$ 14 billion between January and November, based on a trade balance deficit of US$ 3.2 billion and a surplus of US$ 17.2 billion in the financial segment.

14. The upper and lower limits of the exchange float band remained at the levels defined in February (R$ 1.05/US$ for purchase and R$ 1.14/US$ for sale). By the time November came around, the mini float band had shifted by 6.7% and closed at R$ 1.109/US$ for purchase and R$ 1.114/US$ for sale. The rate of exchange in the free segment devalued by 6.8% in the period.

B. Monetary policy in the third quarter of 1997

15. Based on the concept of average daily balances, the restricted monetary base came to R$ 26.2 billion in September and, therefore, well within the parameters defined in monetary programming (R$ 22.7 billion – R$ 26.7 billion), for growth of 30.1% in the year and 51.7% in 12 months. In comparison to September of the previous year, banking reserves turned in growth of 143,6% and currency issued expanded by 22.2%. The higher growth under banking reserves resulted from strong expansion under demand deposits.

16. The balance of the expanded monetary base — including the restricted base, compulsory cash deposits and federal public securities outside Banco Central — totaled R$ 224.3 billion at the end of the third quarter of the year. This result corresponds to percentage growth of 21.9% in the year and 35.9% in 12 months. The balance of the expanded base closed at a level below that defined in monetary programming (R$ 225.8 billion – R$ 265.1 billion) as a consequence of the fact that state debt restructuring operations were not concluded.

Table 1. Observed results and forecast monetary program for the third quarter of 1997

Itemization	Forecast		Observed	
	R$ billion	Percentage change in 12 months 1/	R$ billion	Percentage change in 12 months
M1 2/	33.8 - 39.7	51.3	38.8	59.8
Restricted base 2/	22.7 - 26.7	43.2	26.2	51.7
Expanded base 3/	225.8 - 265.1	48.7	224.3	35.9
M4 3/	340.4 - 399.6	24.4	373.8	25.7

Source: Banco Central do Brasil

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

2/ Working-day balance average of last month in the period.

3/ End-of-period balances.

17. In terms of average daily balances, the money supply (M1) came to R$ 38.8 billion in September and was squarely within the parameters set by monetary programming (R$ 33.8 billion – R$ 39.7 billion), for growth rates of 33.8% in the first nine months of the year and 59.8% in the 12 month period ended in September. In comparison to September of the previous year, demand deposits expanded by 92.6% while currency held by the public expanded by 22.8% in the period. In 1997, the performance of demand deposits has reflected introduction of the CPMF which, in turn, provoked a strong migration of resources out of FIF-CP.

18. the broader concept of liquidity of the economy (M4) came to R$ 373.8 billion at the end of September, quite close to the median point of the parameters defined in monetary programming (R$ 340.4 billion – R$ 399.6 billion). Growth came to 16% in the year and 25.7% in 12 months.

19. Just as in the previous quarter, the TBC and TBAN remained constant at 1.58% and 1.78% per month in the third quarter of the year. The period was also marked by greater convergence of the overnight rate and the TBC, as the effective over-Selic closed at 1.6% per month in July and 1.59% per month in August and September.

C.Monetary policy in October-November 1997

20. Average daily balances of the restricted monetary base came to R$ 26 billion in November, for growth of 29.4% in the year and 54.3% in 12 months. Banking reserves expanded by 200.8% due to sharp 19.9% growth in demand deposits and currency issued, both in comparison to November 1996.

21. The expanded monetary base closed at R$ 220 billion in November, corresponding to growth of 19.7% in the year and 23.9% in 12 months.

Table 2. Observed November and forecast monetary program for the fourth quarter of 1997

Itemization	Forecast		Observed	
	R$ billion	Percentage change in 12 months 1/	R$ billion	Percentage change in 12 months
M1 2/	48.6 - 57.1	82.2	39.2	61.2
Restricted base 2/	31.7 - 37.2	71.2	26.0	54.3
Expanded base 3/	257.7 - 302.5	52.2	220.0	23.9
M4 3/	371.4 - 436.0	25.3	383.0	22.6

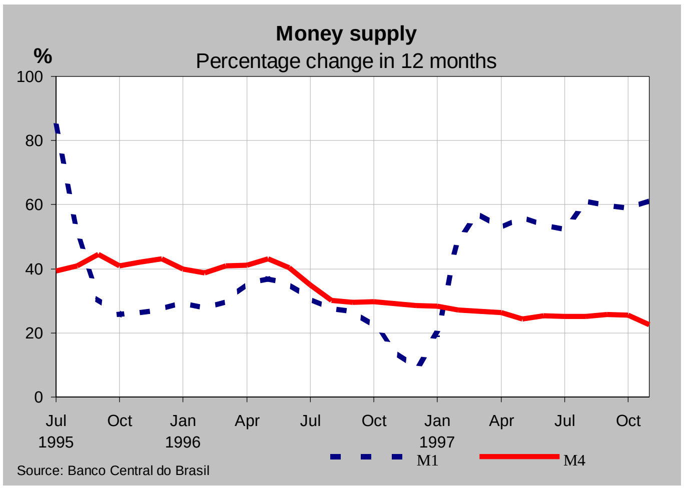
Source: Banco Central do Brasil

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

2/ Working-day balance average of last month in the period.

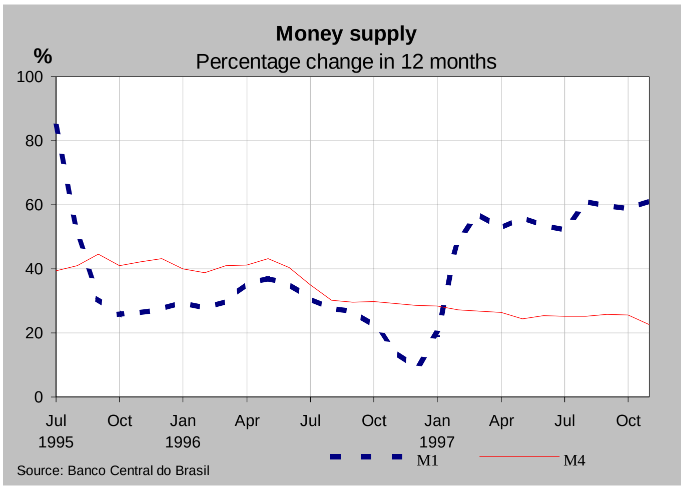
3/ End-of-period balances.

22. The average balance of the money supply (M1) reached R$ 39.2 billion in November, for growth of 35.3% in the year and 61.2% in the last 12 months.



23. The broad money supply concept (M4) totaled R$ 383 billion at the end of November, for accumulated growth of 18.9% in the year and 22.6% in 12 months.

24. The October-November period marked the end of a long period of interest rate stability dating to April of this year. Initially, the TBC and TBAN for October were set at 1.58% and 1.78% per month at the September 17 Copom meeting. The following meeting was held on September 22 and had the objective of defining rates for November. On that occasion, it was decided to reduce the spread between the TBC and TBAN by setting these rates at 1.58% and 1.76% per month. However, the adverse effects of the Asian crisis on the domestic exchange market led Copom to increase basic interest rates to respective levels of 3.05% and 3.23% per month at an extraordinary meeting held on October 30. The new rates went into effect on the following day. Accompanying these shifts, the effective over-Selic rate rose from 1.67% per month in October to 3.04% per month in November. However, once the immediate effects of the crisis had been dissipated and the efficacy of the preventive measures adopted to cope with the situation had been demonstrated, Copom rolled the basic rates for December back to respective levels of 2.9% and 3.15%, at its ordinary session on November 19.



D. Outlook for the first quarter and for 1998

25. During the course of 1997, the fundamental components of the Brazilian economy registered steady improvement. In this sense, production level indicators pointed to continued expansion of economic activity in a framework of increased participation of capital goods output as a result of more intensive investment in the composition of aggregate demand and convergence of the major price indices at very low levels, reflecting the performance of tradables and nontradables. This performance, of course, mirrored the policy of gradual exchange rate devaluation.

26. The strategy aimed at consolidating the process of stabilization had been rooted in an adequate system of financing the current account deficit. In a framework of ample international liquidity, the foreign capital that entered the country gradually adjusted to the time profile required for conclusion of the process of structural economic reform. This led to a situation of effective fiscal balance and, consequently, reduced the need for absorbing the foreign savings required for the investments implicit to a process of sustained growth.

27. As the economic crisis moved beyond the boundaries of Southeast Asia and assumed worldwide dimensions, the fundamental conditions under which economic policy had been implemented up to the end of October changed. With this, following a period of stability dating to April, the government decided to raise basic interest rates with the aim of defending the nation's currency either by avoiding formation of speculative stocks or by making it possible to maintain foreign capital in the country at a time of decreased international liquidity.

28. The more restrictive monetary policy was accompanied by a series of measures aimed at achieving a short-term fiscal adjustment and generating a favorable impact on 1998 fiscal accounts. These measures clearly evince the government's commitment to preserving the gains produced by the stabilization process. However, these measures are not enough but must be accompanied by congressional approval of the structural reforms now under discussion. With this, the restrictions imposed on the economy and which have impacted the activity level will be attenuated to the extent that the growth in internal savings makes it possible to curtail inflows of foreign savings.

29. In this sense, one can presume that the upward trajectory of industrial output will be interrupted in early 1998 when the effects of the restrictive measures will be felt more intensely. Insofar as prices are concerned, expectations are that inflation will be quite close to that of 1997 with a good possibility of being even lower as a result of the short-term adjustment measures recently taken.

30. An analysis of 12 month balances shows that the trade deficit remained relatively stable in the second half of 1997 as a consequence of more dynamic exports and relative stability under imports. In 1998, the trade deficit is expected to close at a significantly lower level than in 1997. The reasons behind this conclusion are the measures recently taken to stimulate exports and, at the same time, aid national companies in their efforts to become more competitive. Another factor to be considered in this context is the impact of the reduction in the level of internal activity.

E. Growth targets for major monetary aggregates

31. Programming for the monetary aggregates in the first quarter of 1998 and their estimates for the end of the year have given due attention to the probable level of inflation, GDP, interest rates, the monetary impacts of National Treasury operations, Banco Central interventions in the exchange market and in the financial system. Table 3 shows the target ranges projected for monetary aggregates at the end of the first quarter and for 1998 as a whole.

Table 3. Monetary program for 1998 [1/]

R$ billion

Itemization	First quarter	Year
M1 [2/]	36.1 - 42.4	48.0 - 56.3
Restricted base [2/]	25.1 - 29.4	32.8 - 38.5
Expanded base [3/]	313.9 - 368.5	372.4 - 437.1
M4 [3/]	406.6 - 477.3	465.6 - 546.5

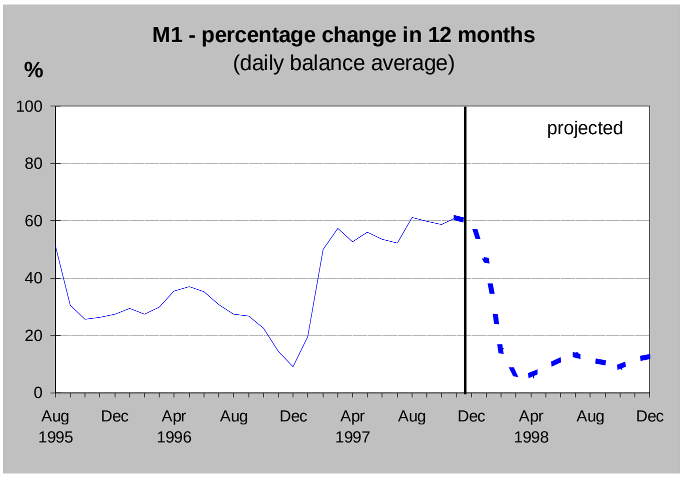
Source: Banco Central do Brasil

1/ Refers to the final month in the period.

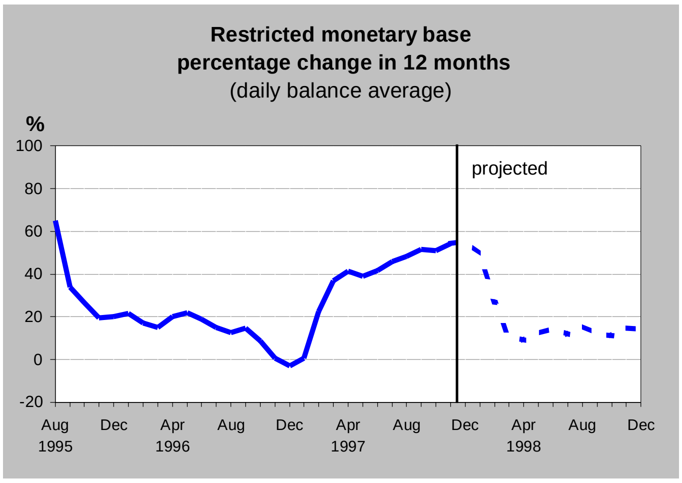
2/ Working-day balance average in month.

3/ End-of-period balances.

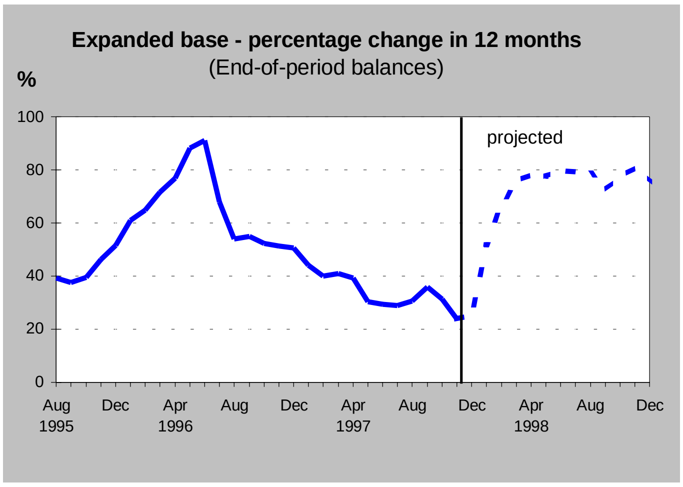
32. By raising the opportunity cost of retaining monetary assets, the increase in internal interest rates generated a reduction in currency demand. Thus, one can expect a reduction in the stock of currency circulating in the economy while the conditions that demand high levels of interest persist. Consequently, the median point of the projection of M1 for the month of March 1998 corresponds to R$ 39.3 billion, or less than the average balance for October 1997 (R$ 39.8 billion). Taking this factor into consideration, one can project 12 month growth in the average daily balance of the M1 aggregate (currency held by the public plus demand deposits) at 6.4% in March and 12.8% in December 1998.



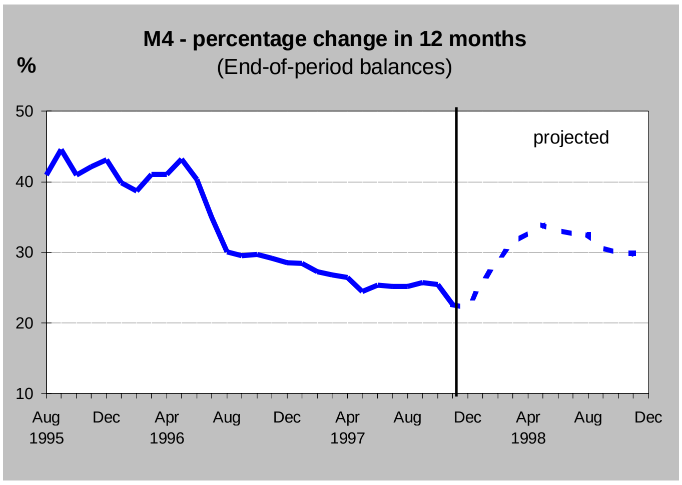
33. Based on the expected performance of currency demand (M1) and the scenario of stability in the levels of compulsory deposits on immediately available resources and of the monetary multiplier, it is possible to project 12 month growth for the average monetary base (currency issued plus banking reserves) at 10.4% in March and 14% in December 1998.



34. In coming months, the major expansionary factor affecting projections of the expanded base (a measurement of the federal internal debt in monetary terms and securities) will be state debt restructuring operations. With this, one can predict 12 month expanded base growth of 75.7% in March and 75.5% in December 1998.



35. In keeping with the performance standard of the other aggregates, one can estimate 12 month M4 growth at 31.4% for March and 28.6% in December 1998.



36. The growth of monetary aggregates is summarized in the following table which presents 1996 results, those of the October/November 1997 period and those forecast for the first quarter and for all of 1998. These data are based on the median point of the forecasts:

Table 4. Evolution of monetary aggregates [1/]

Itemization	1996		1997		1998			
	Year		November		First quarter [2/]		Year [2/]	
	R$ billion	% change in 12 months	R$ billion	% change in 12 months	R$ billion [3/]	% change in 12 months	R$ billion [3/]	% change in 12 months
M1 [4/]	29.0	9.1	39.2	61.2	39.3	6.4	52.2	12.8
Restricted base [4/]	20.1	-3.1	26.0	54.3	27.3	10.4	35.6	14.0
Expanded base [5/]	184.1	50.5	220.0	23.9	341.2	75.7	404.7	75.5
M4 [5/]	322.1	28.5	383.0	22.6	441.9	31.4	506	28.6

Source: Banco Central do Brasil

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.

37. Growth under the various multipliers that is implicit in monetary programming is summarized below:

Table 5. Monetary multiplier [1/]

Itemization	1996		1997		1998			
	Year		November		First quarter [2/]		Year [2/]	
	Multiplier	% change in 12 months	Multiplier	% change in 12 months	Multiplier	% change in 12 months	Multiplier	% change in 12 months
M1 / Restricted base [3/]	1.442	12.6	1.508	4.5	1.440	-3.6	1.464	-1.1
Banking reserves / Demand deposits [3/]	0.232	-53.4	0.387	51.2	0.397	3.7	0.375	-1.1
Currency / M1 [3/]	0.505	18.5	0.365	-24.7	0.417	11.5	0.419	4.2
M4 / Expanded base [4/]	1.750	-14.6	1.738	-26.4	1.295	-25.2	1.250	-26.8

Source: Banco Central do Brasil

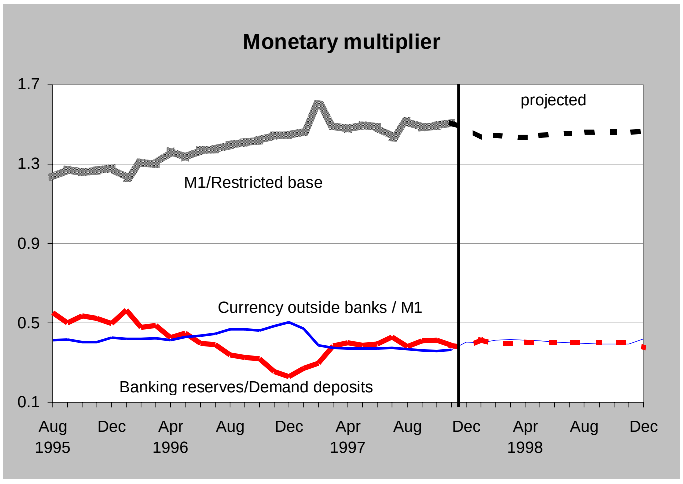
1/ Refers to the final month in the period.

2/ Projected.

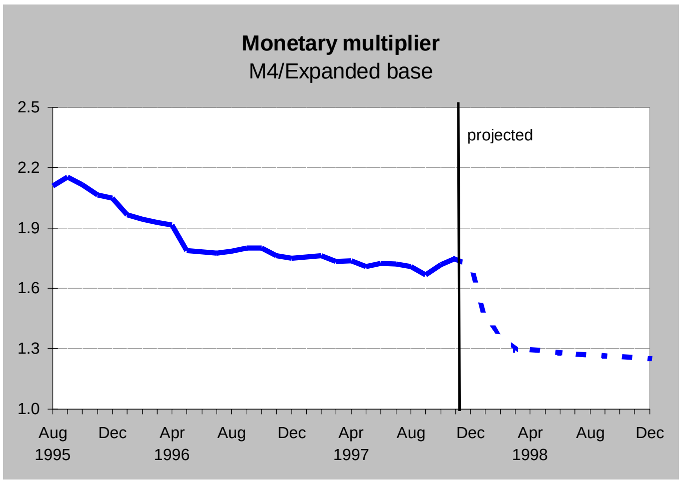
3/ Working-day balance average in month.

4/ End-of-period balances.

38. Now that the country has achieved a relatively long period of price stability, there are no expectations of unforeseen volatility in future values of the restricted monetary base multiplier, even though the process of monetization has not yet ended.



39. In coming months, the expanded base multiplier is expected to decline from current levels, reflecting operations involving restructuring of state debts, since part of these operations will have no impact on M4 despite influencing the expanded base.



Summary of projections

Table 1. Observed results and forecast monetary program for the third quarter of 1997

Itemization	Forecast		Observed	
	R$ billion	Percentage change in 12 months 1/	R$ billion	Percentage change in 12 months
M1 2/	33.8 - 39.7	51.3	38.8	59.8
Restricted base 2/	22.7 - 26.7	43.2	26.2	51.7
Expanded base 3/	225.8 - 265.1	48.7	224.3	35.9
M4 3/	340.4 - 399.6	24.4	373.8	25.7

Source: Banco Central do Brasil

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

2/ Working-day balance average of last month in the period.

3/ End-of-period balances.

Table 2. Observed November and forecast monetary program for the fourth quarter of 1997

Itemization	Forecast		Observed	
	R$ billion	Percentage change in 12 months 1/	R$ billion	Percentage change in 12 months
M1 2/	48.6 - 57.1	82.2	39.2	61.2
Restricted base 2/	31.7 - 37.2	71.2	26.0	54.3
Expanded base 3/	257.7 - 302.5	52.2	220.0	23.9
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Source: Banco Central do Brasil

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2/ Working-day balance average of last month in the period.

3/ End-of-period balances.

Table 3. Monetary program for 1998 1/

R$ billion

Itemization	First quarter	Year
M1 2/	36.1 - 42.4	48.0 - 56.3
Restricted base 2/	25.1 - 29.4	32.8 - 38.5
Expanded base 3/	313.9 - 368.5	372.4 - 437.1
M4 3/	406.6 - 477.3	465.6 - 546.5

Source: Banco Central do Brasil
1/ Refers to the final month in the period.
2/ Working-day balance average in month.
3/ End-of-period balances.

Table 4. Evolution of monetary aggregates 1/

Itemization	1996		1997		1998			
	Year		November		First quarter 2/		Year 2/	
	R$ billion	% change in 12 months	R$ billion	% change in 12 months	R$ billion 3/	% change in 12 months	R$ billion 3/	% change in 12 months
M1 4/	29.0	9.1	39.2	61.2	39.3	6.4	52.2	12.8
Restricted base 4/	20.1	-3.1	26.0	54.3	27.3	10.4	35.6	14.0
Expanded base 5/	184.1	50.5	220.0	23.9	341.2	75.7	404.7	75.5
M4 5/	322.1	28.5	383.0	22.6	441.9	31.4	506	28.6

Source: Banco Central do Brasil
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2/ Projected.
3/ Medium point of forecasts.
4/ Working-day balance average in month.
5/ End-of-period balances.

Table 5. Monetary multiplier 1/

Itemization	1996		1997		1998			
	Year		November		First quarter 2/		Year 2/	
	Multiplier	% change in 12 months	Multiplier	% change in 12 months	Multiplier	% change in 12 months	Multiplier	% change in 12 months
M1 / Restricted base 3/	1.442	12.6	1.508	4.5	1.440	-3.6	1.464	-1.1
Banking reserves / Demand deposits 3/	0.232	-53.4	0.387	51.2	0.397	3.7	0.375	-1.1
Currency / M1 3/	0.505	18.5	0.365	-24.7	0.417	11.5	0.419	4.2
M4 / Expanded base 4/	1.750	-14.6	1.738	-26.4	1.295	-25.2	1.250	-26.8

Source: Banco Central do Brasil
1/ Refers to the final month in the period.
2/ Projected.
3/ Working-day balance average in month.
4/ End-of-period balances.