Inflation Report	Brasília	December 1999	Vol. 1	Nº 3	P. 1 - 133

Inflation Report

Quarterly publication of the Monetary Policy Committee, according to Decree no. 3,088, dated 6.21.99

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Number printed: 1000 copies

Statistical Conventions:

...	data not available.
-	nil or non-existence of the event considered.
0 ou **0,0**	less than half the final digit shown on the right.
*	preliminary data.

Hiphen between years indicates the years covered, including the first and the last year.
A bar (/) between years (1970/75) indicates the average of the years covered, including the first and the last year or even crop or agreement year, when mentioned in the text.

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Foreword

Inflation Report is a quarterly publication of the Banco Central do Brasil with the objective of evaluating the performance of the inflation targeting system and providing a prospective scenario for inflation. The national and international economic conditions underlying decisions taken by the Monetary Policy Committee (Copom) concerning the monetary policy management are presented.

The report is divided into six chapters: Aggregate Demand, Aggregate Supply, International Economy, Capital Account, Prices and Prospects for Inflation. Basically, the analysis of aggregate demand involves consumption, investments, budget operations and the gap of foreign resources. With regard to supply, the analysis is centered on the behavior of the production indicators of the farm and industrial sectors and the labor market. In the chapter dealing with the international economy, the report presents an analysis of the world's major economies and seeks to identify those conditions capable of impacting the Brazilian balance of payments. The next part of the report is a consequence of international economic performance and deals with capital movements, underscoring the ways in which they contribute to meeting foreign payment needs. Price analysis focuses on the results obtained in the quarter as a consequence of monetary policy decisions and the real conditions of economy outside the realm of government action. Finally, prospects on inflation growth are analyzed.

Executive Summary

In 1999, the Brazilian economy has experienced a year of transition. In January, the currency crisis initiated after the Russian moratorium in August 1998, led to the devaluation of the real and to the departure from the managed exchange-rate regime. In June, the government adopted a new monetary policy regime aimed at establishing the economy's nominal anchor: the inflation targeting regime. This new framework led to greater monetary policy rationality and transparency. It also stimulated the discussion on related themes such as the potential benefits of allowing the monetary authority to adopt a preventive stance. Despite the very short period of time that has elapsed since implementation of the new regime, society is already perceiving that policies which do not take into account their long-term impacts are myopic and must be avoided.

However, the fact that best characterizes 1999 may well be the enormous difference between the forecasts made early in the year and the results observed. Forecasts that inflation would surge and that the economy would plunge into a deep recession did not come through. Nonetheless, even the most pessimist analyst did not predict that 1999 would close with a trade balance deficit.

Despite the above, it would still be no exaggeration to state that the transition has been smooth. Inflation, measured by consumer price indices, closed at approximately 9% and the economy will end the year with positive growth in the range of 1%. When one considers the magnitude of the exchange rate shock, the initial expectations, and the experience of the East Asian countries that have been through similar crises, the outcome was surprisingly positive. It is now expected that 2000 will mark the beginning of a sustained growth process.

In spite of the slight growth expected for this year, the industrial sector will most likely close below the 1998 results. The capital goods and consumer durables sectors were hit the hardest since they are very sensitive to credit conditions. The increase in uncertainty, the rising unemployment rate and the high interest rates severely restricted credit supply.

The crop and livestock sector produced results well above those of the previous year. The favorable harvest helped to keep inflation at low levels in the first half of the year, far below than initially expected. This sector also drew important benefits from the exchange rate devaluation as exports of meat, poultry, and related goods moved sharply upward.

The service sector ended up with growth rate similar to that of GDP. It should be pointed out that devaluation fostered internal tourism and investments in the hotel industry. It therefore follows that this sector must experience a significant expansion in 2000.

Even though the good harvest favored the economy, the sharp increase in international oil prices harmed it. Two other negative events were the decline in international commodity prices and Latin America weak growth in 1999. The first, coupled with the hike in oil prices, worsened Brazil's terms of trade. The second had a negative effect on exports of manufactured goods and, particularly, vehicle exports. Hence, the trade balance will close the year with a deficit, albeit much smaller than in 1998.

For the coming year, though, trade balance should improve substantially due to three factors: the effects of exchange rate devaluation will take place with greater intensity; the trend for world economic activity is clearly on the upswing; and the already evident upward movement in commodity prices will further intensify during the year.

One should remember that, in 1999, foreign direct investment was more than sufficient to finance the current account deficit. For the coming year, amortization and interest payment will be substantially lower than in 1999. Together with an improved trade balance performance, this will increase the supply of foreign currency and reduce the current account deficit.

A more vigorous economic recovery, initially expected for the third quarter of 1999, seems to have started only in the last quarter of the year, as suggested by recent indicators. For instance, industrial production rose 1.6% in October driven by consumer durables, capital goods and housing. Such results were leveraged by the credit expansion that intensified in the second half of the year.

In the fourth quarter, there was an unexpected rise in consumer price inflation. For the most part, the increase was due to unanticipated shocks such as the severe beef off-season and the sharp rises in fuel alcohol and automobile prices.

The IPCA upward movement, which closed October at the highest level of the year, caused concern about reigniting inflation. However, in the Monetary Policy Committee´s (Copom) assessment, the economy is not undergoing an inflationary process. Much of the increase in inflation can be explained by the aforementioned shocks, whose effects are basically transitory. Consequently, the inflation rate for December is expected to decrease for the second consecutive month. Similarly, inflation is expected to drop even further in the first quarter of 2000.

The baseline scenario assumes that the adjustment of government managed prices – the major source of concern for next year – will be less intense than in 1999. Sharper growth in the world economy, recovery in commodity prices and lower "Brazil risk" premium shall improve the external outlook and weaken inflationary pressures. Under this scenario and assuming the basic interest rate at 19.0% per year, the forecasted inflation for the coming year is 5.8% and the forecasted GDP growth is 3.5%. Although the central projection for the year 2000 inflation is below the 6% target, there is a probability of almost 50% that inflation rate will reach one percentage point above the targets agreed upon in the Economic Program for the second and third quarters of 2000.

1 - Aggregate demand

1.1 – Consumption

Retail trade

Between April and October, interest rates charged by the retail trade sector fell from 8.9% per month to 7.5% per month. To some extent, this explains why installment sales at the level of the São Paulo retail sales sector declined at a somewhat less accentuated pace than cash sales. Figures on the sector's performance in October, released by the Trade Association of São Paulo, indicate a 9.9% decline in consultations involving cash sales (Telecheque) and a 2.2% reduction under installment sales (Credit Protection Service - SPC). These figures reveal a situation of tighter budgets, coupled with a continued downward trajectory under real wages and earnings.

Real sales of the retail sector - Brazil [1/]

% growth in year

Itemization	1999				
	1st semester	Jul	Aug	Set	Out
General	-4.03	-4.26	-5.02	-4.86	-4.63
Excluding vehicle sales outlet	1.20	1.06	0.37	0.22	0.22
Consumer goods	1.33	1.13	0.36	0.17	0.16
Automotive trade	-29.77	-30.63	-31.40	-30.20	-29.75
Building materials	-6.40	-5.87	-6.13	-5.80	-5.47

Source: FCESP, FCEMG and IBGE (Rio de Janeiro, Recife and Salvador)

1/ Weighted by the 1996 IBGE Annual Trade Survey: São Paulo (53,61%), Rio de Janeiro (24,83%), Belo Horizonte (12,54%), Salvador (5,16%) and Recife (3,86%).

In a framework of five metropolitan regions, the indicator of real sales in the retail trade sector declined by 4.6% up to October. One of the major factors in this result was the weak performance of the automotive industry. When factory sales outlets are excluded, the indicator suggests a tendency toward stability. In accumulated terms for the year, real sales closed with a negative result in all the regions analyzed. The strongest negative results occurred in Recife and Belo Horizonte, with respective reductions of 12.8% and 12.4%, followed by Rio de Janeiro, São Paulo and Salvador. One should stress that participation of factory outlets in overall retail sales was more significant to the São Paulo results, where the decline of 3.4% is altered to a growth of 3.9% when vehicle sales are excluded.

In the month of October, real sales of the retail trade sector in the metropolitan region of São Paulo - expressed on the basis of Depec's seasonally adjusted series - expanded by 1.6%, with growth of 3.6% in real sales of consumer goods, principally consumer durables (7.2%). One of the major reasons underlying this expansion was the recent interest rate reduction. In the segment of nondurables, real sales expanded by 0.5%, while marketing of semidurable goods dropped by 1.2%. Even more accentuated declines occurred under automotive sales: 4.2% drop in factory outlet sales and 3.3% under auto parts and accessories. The sector of building materials registered positive sales for the second consecutive month, with 3.9% in September and 2.7% in October.

When one considers the accumulated results for the year, overall retail trade operations in the metropolitan region of São Paulo closed with a decline of 3.4%. When sales at factory vehicle outlets are excluded, the period closes with positive 3.9% expansion. The highest rates of growth occurred under auto parts (14.5%) and nondurable consumer goods (12%), principally supermarkets (13.1%). At the same time, consumer durables and semidurables ended with falloffs of 2.8% and 11.1%, respectively.

Automotive vehicles

Demand for consumer durables dropped sharply in 1999, mostly as a result of reductions in real income and sharp upward movement in interest rates at the start of the year. According to figures released by the National Association of Automotive Vehicle Manufacturers (Anfavea), automobile industry sales up to November declined by 10.2% when compared to the same period of the preceding year.

Based on data seasonally adjusted, total sales in the September-November quarter fell by 0.9% when compared to the immediately previous quarter. One should note that the September result was impacted by termination of the Automotive Sector Emergency Agreement on the 30th of the month. This agreement had entitled the sector to an industrialized products tax (IPI) rate reduction. Internal market sales in November expanded by 0.5%, with an accumulated drop of 10.2% in the year, while vehicle exports declined by 20.4%. Viewed as a whole, the overall falloff for the year came to 40.1%. Vehicle imports diminished by 1.4% in October and 56% in the year.

Vehicle sales, stocks and imports

% monthly growth

Itemization	1999				
	Jul	Aug	Sep	Oct	Nov
Sales 1/	12.9	2.2	-2.2	-7.7	3.1
Internal	8.9	7.2	-1.2	-10.3	0.5
External	4.5	5.9	-4.1	4.0	20.4
Imports 1/	-16.0	-2.0	5.1	-1.3	...
Stocks	-2.6	0.2	9.1	3.2	...

Source: Anfavea, Ministério da Fazenda and Fenabrave

1/ Seasonally adjusted data.

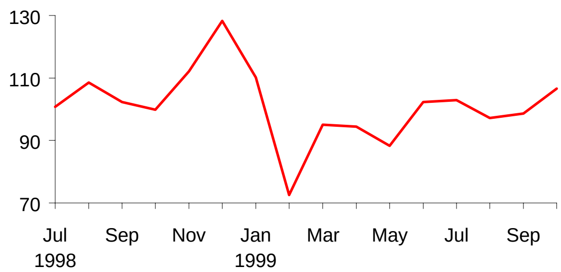
As expected, the performance of factory sales outlets was quite similar to what occurred at the level of the industry itself and was marked by a favorable reaction at the moment that the aforementioned agreement went into effect and at the announcement of the final date for its termination. This is evident in October results, when total sales fell by 20.4%. A breakdown of these figures shows reductions of 33.1% in the segment of buses, 29.7% under light commercial vehicles, 18.9% under passenger cars and 14.9% in the truck segment. The only heading to register positive growth was output of farm machines (4.7%).

Electric-electronic goods

Industrial sales of electric-electronic goods

Seasonally adjusted data

1994=100

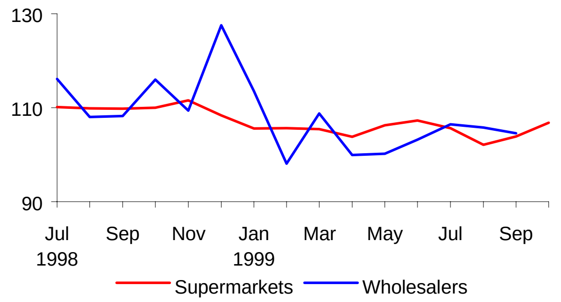


Analyzed on the basis of data from which seasonal factors have been eliminated, a comparison of average sales of the electric-electronic goods industry from July to October with that of the first half of the year indicates growth of 8%. With this result, the accumulated decline in the year diminished from 18% up to June to 13% up to October. On a segment-by-segment basis, sales of image and sound equipment registered the highest decline (28.9%), while sales of portable products and home appliances dropped by respective rates of 6% and 4% in the same period.

Supermarkets and wholesale trade

Brazil (real sales)

1995=100



Source: Abras and Abad

Supermarkets and wholesale trade

According to a survey by the Brazilian Association of Supermarkets (Abras), real supermarket sales diminished by 2.9% up to October, when deflated by the General Price Index - Domestic Supply (IGP-DI). Once seasonal factors are weeded out, the final results point to declines in July and August and positive growth of 1.7% in September and 2.8% in October. With this, average sales in the second half of the year were 1% below the result for the first six months.

In much the same way, real sales in the wholesale trade sector - deflated by the Wholesale Price Index - Domestic Supply (IPA-DI) - closed with downward movement reflected in a drop of 1.1% in the year up to September.

Fuel consumption

When compared to the same 1998 period, apparent consumption of petroleum derivatives increased by 0.3% up to October. This result was generated by expanded demand for liquid petroleum gas (3.8%) and diesel oil (0.3%), and reductions in consumption of fuel oil (7.1%) and automotive gasoline (6.2%). According to data up to September, consumption of fuel alcohol dropped by 3.4%.

Credit cards and check clearing

Demand indicators reflected in the volume of credit card operations and the number of checks cleared produced sharply differentiated results over the course of the year. To some extent, this was due to more intensive utilization of credit cards. Final figures up to October show that credit card operations expanded by 21.4%, while operations paid with checks declined by 4%. When these figures are brought together, the overall number of transactions rose 1.7%, a level compatible with the pace of activities in the period.

Defaults

In the retail trade sector of the metropolitan region of São Paulo, the default level has been relatively stable in recent months. According to the São Paulo Trade Association, the net rate moved from 8% in

September to 8.5% in October, before dropping back to 8.1% in November. In Rio de Janeiro, the indicator measured by the Teledata system, which determines the ratio between checks returned and total checks received by the trade sector, continued on a downward curve during the year with levels of 1.92% in August, 1.84% in September and 1.62% in October.

In just the opposite sense, the nationwide index that defines the ratio between checks returned for insufficient backing and check clearing operations moved upward during the year. In October, the figure came to 3.59%, in comparison to 3.26% in September and a 2.46% average for the first half of the year. Another sign of an expanding default level is evident in a comparison between the average up to October 1998 (2.67%) and that of the same period of this year (2.82%).

Buyer-groups

In comparison to the same 1998 period, the number of buyer-groups declined by 12.8% up to October, following a 13.5% reduction in the first half of the year. In much the same way, vehicle buyer-groups diminished by 16.6% up to June and 13% up to October, while those focused on acquisitions of different types of equipment (tractors, farm and highway equipment, cargo and mass transit vehicles, aircraft and vessels) remained relatively stable.

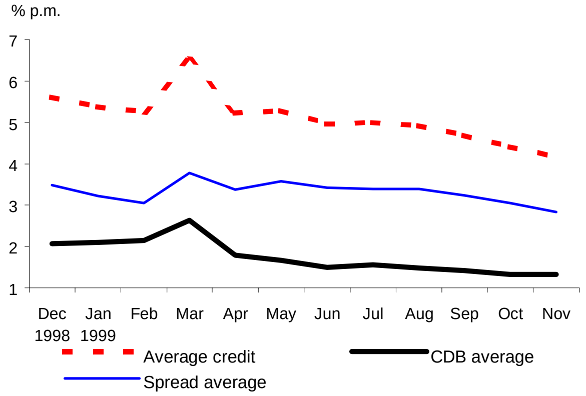
1.2 – Credit

The basic orientation of the nation’s credit policy is to fostering growth through implementation of mechanisms that will make it possible to reduce the costs of financial intermediation and expand the availability of credit. Among the factors that contribute to this objective, one should stress the reduction in compulsory deposits on financial investment funds and demand and time deposits, together with the cutback in the IOF rate charged to individuals. In this way, it is hoped that the channel of monetary policy transmission through credit will play an increasingly more important role in the process of economic growth recovery.

Insofar as financial system cost reductions are concerned, one should cite creation of the Bank Credit Bill, which can be described as a credit security that can be more efficiently and effectively executed in court. At the same time, the minimum value of the contracts financial institutions are obligated to register in the Central Risk System was cut from R$ 50 thousand to R$ 20 thousand.

Going on to the credit supply, more favorable conditions were created for working capital lending operations. These transactions were concentrated in Banco do Brasil and the Federal Savings Bank and utilized funding from the PIS/Pasep Participation Fund. Parallel to this, the Fiscal Recovery Program (Refis) was created, with the objective of normalizing federal government credits involving business tax and contribution debts that had barred these firms from signing new contracts with development agencies.

Spread of credit operations

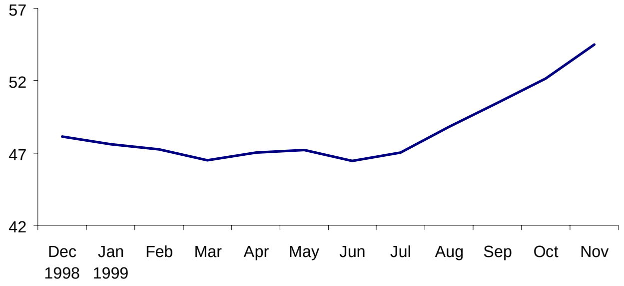


In this scenario of growing liquidity and the possibility of cost reductions, credit operations increased at the same time in which the banking spread narrowed in relation to the average rates on bank deposit certificates (CDB). With this, the monthly average of the differential between the lending and borrowing rates of the financial system moved from 3.3% per month in July to 2.8% per month in November, for an annual rate of 47.1%, as against 39.8%.

The August-November period registered downward movement in the median spread in all types of regular credit operations. The most accentuated falloff occurred under operations with individuals, in which the monthly average spread declined from 5% per month in July to 4.2% per month in November. In annual terms, this meant a reduction of approximately 14%. In that segment, the most remarkable reduction occurred under spread on overdraft check, dropping from 7.2% per month in July to 6.3% per month in November. In annual terms, this rate dropped from 129.4% to 109.3%. Under personal credit, the monthly average dropped from 4.7% to 3.9% while annual average declined from 73.6% to 58.4%.

In the case of business credits, the average monthly spread narrowed from 2.3% in July to 2.1% in November, annually declining from 31.8% to 28%. In monthly average terms, insofar as growth in the type of spread is concerned, there has been a reduction from 2.7% to 2.3% in hot money; from 2.8% to 2.3% in the discounting of commercial invoices; and from 2.3% per month to 1.9% in working capital operations. In annual terms, rates dropped from 37.2% to 30.7%; from 38.9% to 32% and from 31.2% to 25.1%, in the same order as above.

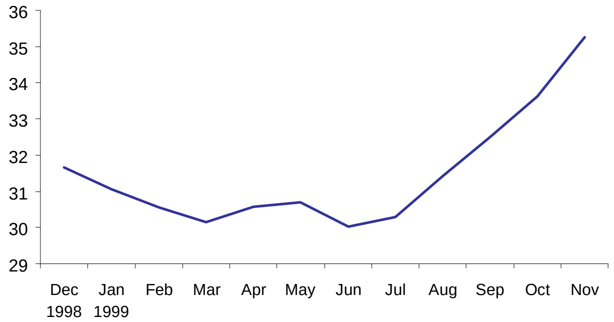
Amount of credit operations (individuals + legal entities)
R$ billion



1/ Daily average balances.

When real estate, rural, leasing and public and foreign fund credit modalities are excluded, the volume of credit operation onlendings expanded by 15.8% in the August/November period and by 13.2% in comparison to December 1998. Of this total, operations contracted with legal entities expanded by 16.4% in the period and 11.3% in the year, while those carried out with individuals expanded by respective rates of 14.8% and 16.8%.

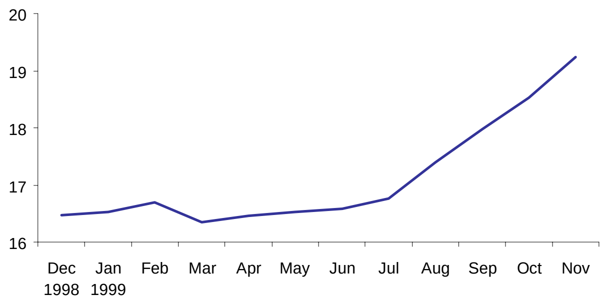
Amount of credit operations with legal entities[1/]
R$ billion



1/ Daily average balances.

In the business segment, vendor operations increased by 29.6% and closed at R$ 3.7 billion, while commercial invoice discounting expanded by 22.6% to R$ 3.1 billion. Positive growth also occurred under promissory notes, with expansion of 31% and a total of R$ 521 million; acquisitions of goods, with growth of 24.4% to a volume of R$ 1.1 billion: and operations through overdraft accounts, with expansion of 26.5% to a level of R$ 11.7 billion. In the same direction, working capital operations increased by 4.8% and closed at R$ 14.4 billion, while hot money operations expanded by 18.3% to R$ 683 million.

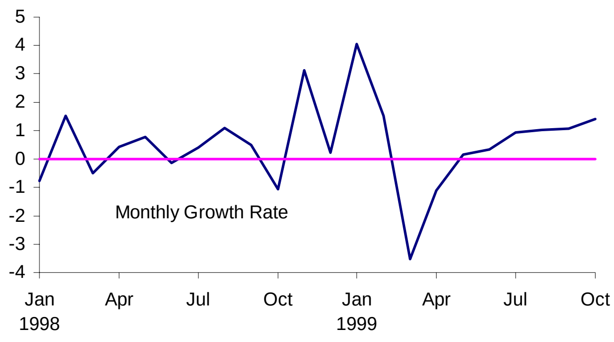
Amount of credit operations with individuals[1/]
R$ billion



1/ Daily average balances.

With regard to operations with individuals, the volume of personal credit operations increased by 20.7% and closed at R$ 8.7 billion; credit operations

Financial System Loans : Private Sector

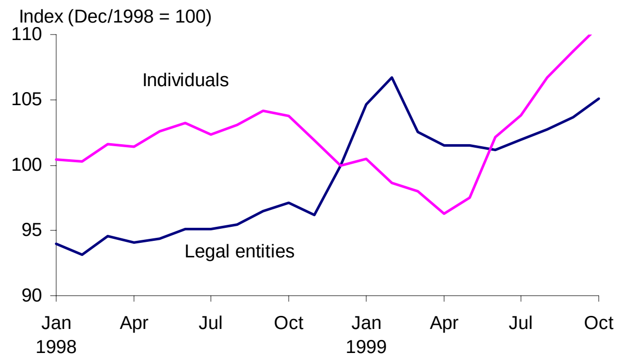


targeted to acquisitions of goods increased by 11% to a level of R$ 4.7 billion; special overdraft check operations increased 9.8%, coming to R$ 5.8 billion.

With regard to the stock of loans granted by the financial system to the different segments of activity has been expanding at a moderate pace since July, without generating any undue pressure on aggregate demand. Total normally performing loans increased by 3.2% in the August-October quarter, closing with a total of R$ 268.4 billion, for an accumulated increase of 5.3% in the first ten months of the year.

A breakdown by sectors shows that total public sector credits came to R$ 33.8 billion in October, with expansion of 1% in the quarter and 2% in the year. Loans contracted by the federal government increased by 3.4% in the August-October quarter and climbed to a level of R$ 6.3 billion. To some extent, this result reflects exchange indexing of contracts in the month of August; liquidation of a share of the debts of state service companies in September; and operations involving the granting of advances on exchange contracts to public companies involved in industrial activities in October. The state and municipal banking debt closed with a balance of R$ 27.4 billion, for growth of 0.5% in the quarter. For the most part, this growth can be credited to releases of funding for the financing of public transportation systems.

Growth in Loans of the Private Financial System



Credit operations contracted by states and municipalities remained stable during the course of the year, demonstrating that the restrictions imposed on these operations as part of the process of adjusting public sector spending are achieving their objective. In more specific terms, the balances of these operations were not permitted to exceed the amounts registered on 9.30.97, indexed monthly by 80% of the Reference Rate (TR). Aside from this, starting in the month of October, credit operations are to be limited to 45% of adjusted net worth of the financial institution granting the credit, with an overall value limit of R$ 600 million for new contracting operations.

Insofar as the private sector is concerned, credit operations added up to R$ 234.6 billion in October, for growth of 3.5% in the quarter and 5.8% in the year.

Credits contracted by individuals totaled R$ 33.4 billion in October, for growth of 6.6% in the quarter and 10.6% in the year. Since the month of May, this has been the most rapidly expanding market segment particularly in terms of the volume of personal credit operations and the increase in the contracting of financing for acquisition purposes.

Insofar as loans to legal entities are concerned, the balance of credit operations totaled R$ 201.2 billion in October, with growth of 3% in the quarter and 5.1% in accumulated terms for the year.

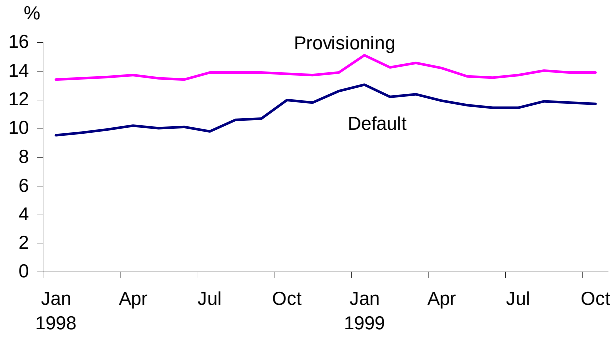
Commercial credits aimed at making operations with durable consumer goods feasible totaled R$ 20.3 billion in October, for increases of 8.6% in the quarter and 12.2% in the year. The balance of loans related to other services closed at R$ 28.6 billion, with growth of 4.7% in the quarter and a falloff of 10.6% in the year.

The balance of loans granted to industry climbed to a level of R$ 71.2 billion in October, for quarterly growth of 4.3%. In the year, growth came to 18.9%. To some extent, this performance reflects the early 1999 impact of exchange devaluation on the indexing of contracts tied to the dollar. Parallel to this, factors with a particularly strong impact in the month of September include investment financing and advances on exchange contracts to the productive sector, granted by the public financial system.

Credits channeled to the housing sector came to a balance of R$ 60.1 billion, reflecting a decline of 1.5% in the quarter and 1.2% in the year. For the most part, this was a result of lesser demand for financing of new real estate.

Based on the Wage Variation Compensation Fund (FCVS), authorities initiated a process aimed at stimulating liquidation of housing finance contracts. This effort resulted in a drop in the balance of financing channeled to the housing segment, while also improving the profile of the financial system’s loan portfolio. It should be noted that the

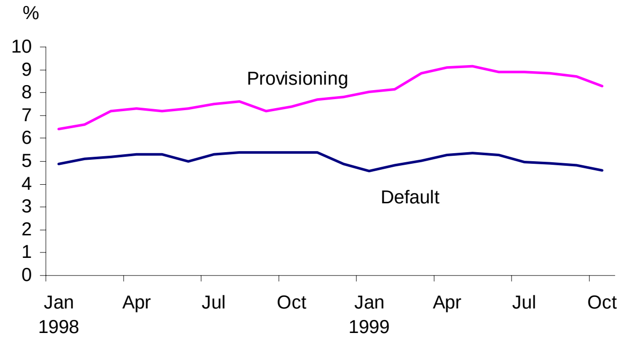
Default and provisioning of the Public Financial System



contractive impact of such operations on aggregate demand is substantially less than the volume of canceled credits as a result of the discounts offered to clients willing to pay off their balances.

The balance of financing granted to the rural sector came to R$ 21 billion in October, for growth of 5.2% in the quarter due mostly to disbursements made to meet demand for current expenditure credits for the 1999/2000 summer harvest. In accumulated terms for the year, growth came to 1.5%. Here, one should note that between the months of April, the month of heaviest concentration of marketing loans for farm products, and August, the credit balance declined as a result of amortizations of these loans and a lag in defining budget resources to be used by the National Treasury in interest rate equalization operations.

Default and provisioning of the Private Financial System



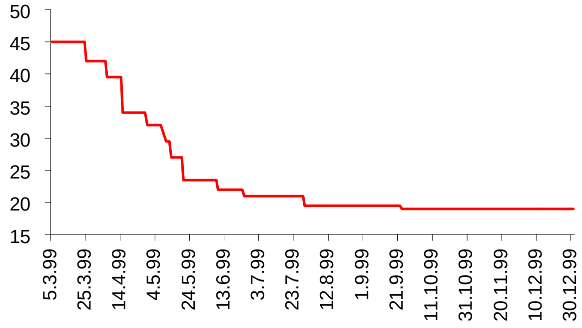
The balance of credit operations in arrears and in liquidation, less income to be appropriated, totaled R$ 25.3 billion in October and corresponded to 8.6% of total credits, as compared to an average of 8.9% in the first ten months of the year. Provisions for hard-to-recover credits came to R$ 33.6 billion or 33% above the balance of credits in arrears and in liquidation.

Insofar as the private financial system is concerned, the default rate continued along a downward curve in the August-October quarter and closed at 4.6%. The cautious approach adopted by the institutions involved in this sector of activity has avoided deterioration in their credit portfolios, principally in the case of contracts indexed to foreign exchange, one of the modalities that had contributed significantly to the increase in default rates in the first six months of the year. Provisions set aside by the sector came to 8.3% of total credits.

In the public financial system, the participation of credits in default in total credits has remained stable over the past six months and closed October at 11.7%. The provisions set aside in the period have remained at a margin of approximately 18.8% in relation to credits in arrears and in liquidation.

1.3 - Monetary policy

Selic rate target
% p.y.



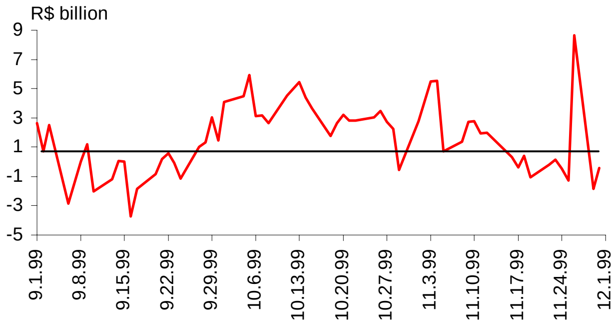
Monetary policy in the second half of the year has been marked by continued downward movement in basic interest rates, albeit at a lesser pace than in the second quarter of the year, in compliance with the inflation target policy.

At its September 22 meeting, Copom took these factors into account and decided to lower the Selic interest rate target from 19.5% per year to 19% per year. In the following three meetings, held on October 6, November 10 and December 15, the Committee did not alter the 19% annual rate. The only difference in relation to the September meeting was that it adopted a downward bias for October while no bias were adopted in the following two months.

At the same time, the monetary authority recognized the need to foster economic growth through increased private spending. To achieve this, it took measures to reduce the lending rates levied by the financial system, while also seeking to reduce the banking spread by lowering costs and attenuating the risks inherent to intermediation operations.

With regard to cost reductions, steps were taken to lessen the Financial Operations Tax (IOF) rate on loans to individual consumers to 1.5%, the same rate applied to business credit transactions.

Free available funds of the banking system



With the same end in mind, the monetary authority reduced the level of compulsory reserves. Reserves on time deposits, which are set aside in the form of securities, were gradually lowered from 30% up to May 5 until reaching zero on October 22. In this context, the securities earmarked to Banco Central, which were incorporated into the free portfolio of financial institutions, declined by approximately R$ 27 billion, enhancing financial system's flexibility in channeling these resources.

Starting in the month of October, the compulsory reserve rate on demand deposits and deposits subject to notification was reduced to a level of 65%. The previous rate was 75% and had been in effect since January 1997. In this case, the release of monetary resources increased by approximately R$ 2.7 billion the banking system's free available funding, defined as the sum of free available resources plus the monetary authority net financing position backed by federal securities.

One should emphasize that the available funding originally generated as free banking reserves required compensatory monetary authority intervention with the aim of avoiding the possibility of liquidity levels higher than those required by the market pressuring interest rates. Consequently, the Banco Central position in federal security financing, which had registered a low average value in September, closed October with an average of R$ 3.4 billion in financing operations. This position was adjusted over the course of the month through net placements of federal securities in definitive operations totaling R$ 3 billion. In the month of November, significant available resources were registered only in the first fifteen days of the months, as a result of disbursements against the National Treasury single account in the period.

Among the measures aimed at attenuating the risks involved in financial intermediation, one should cite more flexible maturities, rates and indexing factors in financial system operations. The purpose of these measures is to facilitate the task of making the terms and rates of lending and borrowing operations compatible and, consequently, reducing market risks. Aside from this, credit risks were attenuated by expanding the coverage base of the Risk Center, with reductions in the minimum limit of credit operations subject to notification and creation of the Bank Credit Bill. This latter item remains as a provisional measure to be approved by the Congress.

One should also underscore the highly important implications of the measures announced by Banco Central and the National Treasury on November 4. The aim of these steps was to streamline the operations of the federal securities market, giving it a more dynamic character and making it possible to reduce the financial costs of debts and increase their duration.

The lengthening of terms coupled with reduction in premiums on issues of federal securities may well have a favorable impact on the credit conditions offered by the financial system, to the extent that the instruments used to obtain funding incorporate the positive effects consequent upon alterations in the profile of federal instruments.

One should note that some procedures aimed at expanding the liquidity of the federal securities market have already been adopted, such as the concentration of maturities, as evident in the recent LTN auctions held on November 4, 11 and 18, when these papers were offered with maturity on May 3, 2000. In the same sense, a measure that has been in effect since August extended to individuals and all legal entities the possibility of carrying out committed operations with any types of securities and any time frames, provided that earnings or profitability parameters are stipulated on the date of contracting. Until this measure went into effect, security operations with repurchase/resale commitments by unauthorized individuals and legal entities could only be carried out for a minimum of 30 days with backing in federal papers.

Interest rates and market expectations

Using the Selic rate as the parameter, real interest rates in the January-November period varied between 15% per year and 17% per year, when consumer price indices are considered. When general price indices are used as deflators, real rates oscillated in the range of 4% per year to 6% per year, the lowest levels since implementation of the Real Plan.

Real interest rates

%p.y.

Period	Deflator						
	IGP-DI	IGP-M	IPA-DI	IPC-BR	INPC	IPC-Fipe	IPCA
1995	33.38	32.84	43.91	21.58	25.50	24.29	25.06
1996	16.54	16.69	17.87	14.43	16.77	15.78	16.29
1997	16.09	15.82	15.76	16.37	19.59	19.04	18.59
1998	26.62	26.52	26.88	26.67	25.66	31.13	26.69
1999 [1/]	4.68	5.23	-2.79	15.88	16.30	15.74	15.53

1/ January to November average, in annual terms.

In early November, the reduction in the pace of interest rate decline and indication of no bias by the Monetary Policy Committee, and the disclosure of higher than expected inflation figures led the market to re-estimate its interest rate expectations. At the end of the month and throughout December, these expectations turned around, as a result of improved domestic and external indicators, such as lower inflation rate prospects for next year and the consolidation of significant fiscal results. This posture becomes evident when one analyzes the Selic rate and the interest swap market with maturity in one year. In

Secondary market

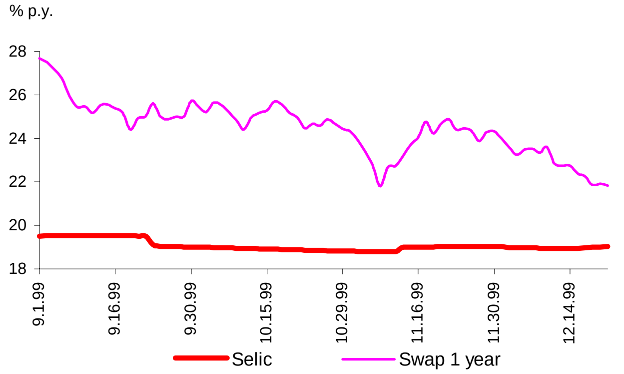
Banco Central do Brasil and the National Treasury announced a series of measures aimed at overhauling the federal public securities market, with particular emphasis on secondary market operations. The conditions for rolling over the public debt will be impacted, in a context of growing liquidity and market transparency. The following measures are expected to generate the most direct impacts on the costs and duration of the public debt:

- issue of long-term preset papers with a competitive offer of a sales option. This procedure is equivalent to offering insurance against unanticipated price fluctuations:
- allow the Selic rate to fluctuate more freely around its current target. This procedure will discourage institutions from reducing their banking reserve market positions to zero as a consequence of the greater interest rate risk, while increasing market demand for definitive operations with federal securities;
- public offers of long-term preset papers, following reception of a firm purchase proposal from financial institutions, representing their clients;
- regular and predetermined National Treasury purchase auctions involving the institution’s own papers, in such a way as to use these operations as an instrument for altering the quality of Treasury debt on the market; and
- permission for separate negotiation of the principal and coupons of exchange securities.

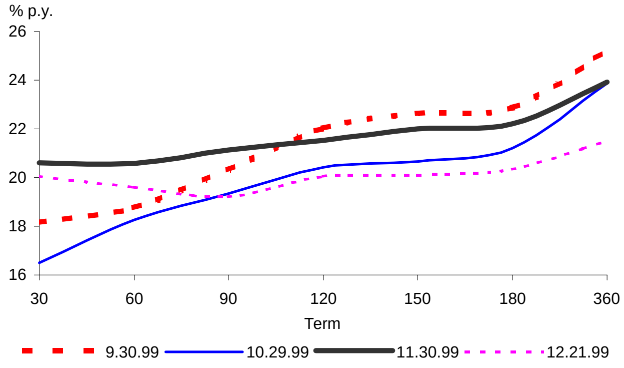
With regard to the measures taken to expand market liquidity and transparency and, in this way, reduce premiums on federal security placements and lengthen the debt profile, one should underline the following:

- offering of prefixed securities, with repurchase commitment, in order to cover financial institutions' short sales;
- reduction in the number of federal security maturities, avoiding the possibility of public offers competing with secondary market operations, since a large number of maturities is detrimental to the process of price formation and diminishes the liquidity of the paper in question;
- more frequent federal security purchases and sales in definitive secondary market operations;
- development of a system of Selic registration of forward federal security operations, thus making it possible to formalize these operations more simply and directly;
- carrying out of federal security operations in Selic with liquidation in D + 1 and incentives to the utilization of electronic systems in negotiating federal securities. Such procedures are aimed at stimulating market participation on the part of new economic agents, such as individuals and nonfinancial legal entities;
- daily publication by Andima of the price quotations of preset and exchange securities; and
- prior National Treasury release of a schedule of security issues in public offers. The first of these was published on November 25 with the December schedule.

Selic x Swap 1 year



Yield curve - swap prefixed



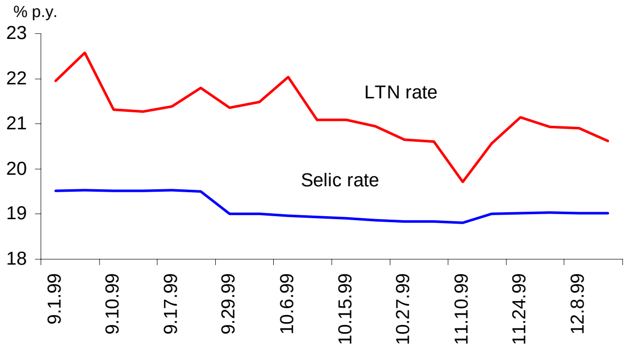
this latter case, a slight increase was observed in November, when rates decreased to a level around 22% p.y. in mid-December.

The change in expectations can also be shown by shifting and rotating the forward structure of interest rates. Rates projected over a period of one year through swap contracts came to 21.5% on December 21, as against 25% at the end of September. Short-term contracts registered growth in their projections at the end of November, thus suggesting that agents had come to the conclusion that a short-term increase in interest rates was probable, though this would not contaminate expectations over a longer temporal horizon. In December, considering rates negotiated on the 21st, a reduction of 2 percentage points is observed for contracts with terms longer than 90 days.

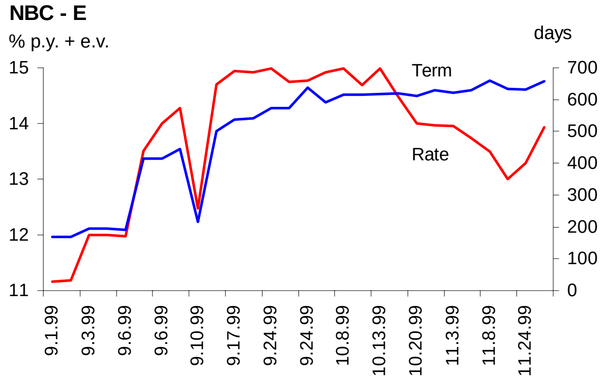
Federal public securities

Definitive operations with federal securities between September and November were aimed at ensuring the continuity of the management process of the federal securities debt. Consequently, Banco Central effected net redemptions of R$ 16.3 billion in the period, while the National Treasury made net sales of R$ 16 billion.

LTN - 3 months



In the September-November quarter, the National Treasury carried out auctions of preset papers (LTN) and papers indexed to the over/Selic rate (LFT). In September and October, LTN terms came to about three months before widening to five to seven months in November. It should be noted that the increase in the terms of preset papers represents gains for both monetary and fiscal policy as a result of growth in the average duration of the federal securities debt.



Average placement rates for shorter term preset papers fluctuated between 0.9 and 3.1 percentage points per year above the Selic rate in effect on auction days. In their turn, preset papers with terms in the range of six months registered average placement rates of 1.9 to 4 percentage points per year above the Selic rate in effect on auction days.

From September to November, placements of Banco Central papers through auctions were limited to NBC-E, which are papers indexed to exchange variations. In the first of these months, placements added up to approximately R$ 3 billion with the objective of meeting demand for papers of this type. In October and November, the volume of exchange securities placed was sufficient only to cover the redeemed flow.

Starting on October 28, the ceiling on the sold positions of financial institutions was abolished. By releasing demand for investments in assets tied to the rate of exchange, this measure has a beneficial impact on net placements of this type of security.

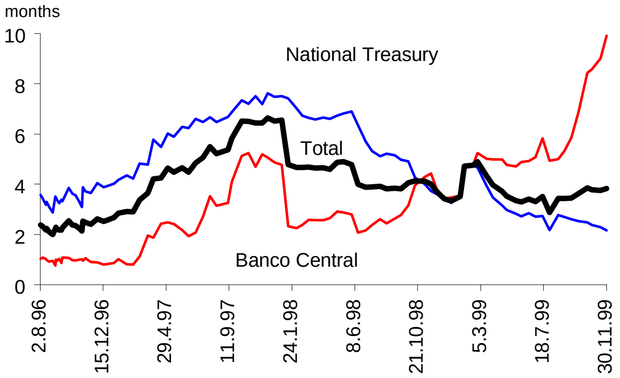
NBC-E placement rates declined in the period, as a result of diminished pressure on exchange markets after the monetary authority intervention in September. In that month, internal rates of return on business days came to more than 15% per year in comparison to the November average of 13.7% per year, despite the fact that the terms of these papers had been lengthened.

Starting in the month of December, the National Treasury carried out public offers of NTN-C, a security indexed to the IGP-M with half-year coupons of 6% per year. The first auction occurred on the first of December and involved two lots of R$ 1 billion each. One of these had a maturity term of three years while the other had a term of seven years, with a single price for all the accepted proposals. In these auctions, specific modalities of securitized credits registered at Cetip and for which the National Treasury is liable were accepted as payment.

The volume of NTN-C with three year maturities came to R$ 675 million, with a rate of 12% per year, while placements of papers with seven year maturities totaled R$ 325 million and generated 12.5% per year. Of total securities placed, 21% were liquidated with securitized credits, with an average discount of 15% over their face value.

Reintroduction of NTN-C and acceptance of federal securitized credits for payment purposes have the aim of strengthening the long-term parameters of the Brazilian economy as related to interest and inflation and reducing the modalities of federal securities in circulation, in such a way as to raise secondary market liquidity; and offering instruments that can be used as backing for long-term liabilities.

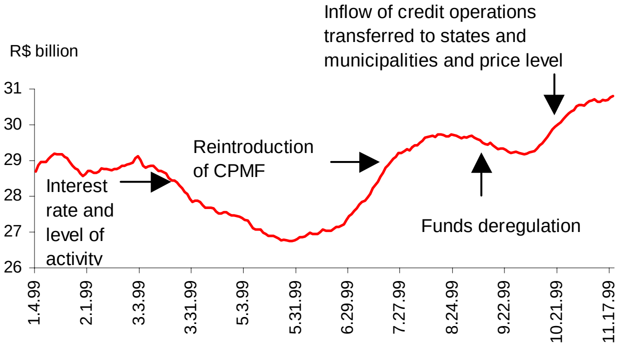
Average duration



After reaching a level of 2.87 months on July 30, the lowest level since February 1997, the average duration of federal securities issued in public offers moved to 3.8 months on November 30, thus suggesting an upward trend under this indicator. For the most part, this recovery can be attributed to growth in the participation and redemption terms of exchange securities on the market.

Monetary aggregates

Demand deposits - 21 days moving average



In the restricted concept, average daily balances of the money supply declined by 1% in September in comparison to the preceding month. To some extent, this result can be attributed to migration of resources to investment funds, which had become more attractive as a result of the deregulation process undertaken from August onward.

In October and November, currency demand increased by 3.2% and 2.1%, respectively. Among the factors responsible for these increases, the most important were price rises during the year, greater availability of credit and growth in federal government transfers to states and municipalities. One should note that the income velocity of the aggregate in November closed at the level registered in the same month of the previous year, when considered from the point of view of the concept of the monthly average of daily balances.

Duration

Created in 1938 by the financier Macaulay as a business finance indicator, the concept of duration only gained prominence in the 1970s and became a component of macroeconomic analyses. The concept expresses the price sensitivity of a preset paper to interest rate changes. This concept has substituted that of average maturity, now considered an inadequate measurement of the price sensitivity of a specific security since it does not take due account of the effects of the payment of coupons and intermediate amortizations of a security.

The concept was initially proposed as a way of standardizing future cash flows by making papers with coupons and intermediate amortization compatible with preset papers in terms of their respective time frames. Duration makes it possible to add together time periods of differentiated cash flows. Macaulay's concept of duration depends on three factors: the remaining redemption period of the security, the payment flow of the coupons and the paper's rate of earnings, expressing the effective life of a security in terms of time.

By weighting the average reception term of the financial flows by the current value of these flows, Macauley managed to resolve the deficiencies encountered in the concepts of maturity and average term so as to be able to compare papers with differing characteristics. Taken by itself, maturity measures the time period for receiving the principal and, consequently, the length of the period during which the holder of the paper will be exposed to the risk of interest rate variations that could devalue future cash flows. By ignoring the value of intermediate coupons, which can be reinvested at current interest rates, maturity tends to become even more inappropriate for measuring the price sensitivity of a paper as the value of the coupon increases.

In order to elaborate a percentage estimate of the price sensitivity of a security to changes in interest rates, the most commonly used concept is that of modified duration, obtained by applying the ratio between Macaulay's duration and the paper's rate of earnings. However, since this is a linear measurement, modified duration applies only to very small interest rate variations and tends to generate deviations between effectively observed elasticity and that forecast by the formula. The greater the interest rate alteration, the greater the deviations. For purposes of macroeconomic analysis and in light of these imprecisions, Banco Central has been utilizing Macaulay's original concept of duration instead of that of modified duration as an approximate measurement in units of time of the sensitivity of the federal debt issued in public offers to interest rate changes. In this way, the greater the duration of the debt, the greater will be the presetting of its rates and, therefore, the greater will be the impact of a given interest rate alteration on the financial portfolio of agents.

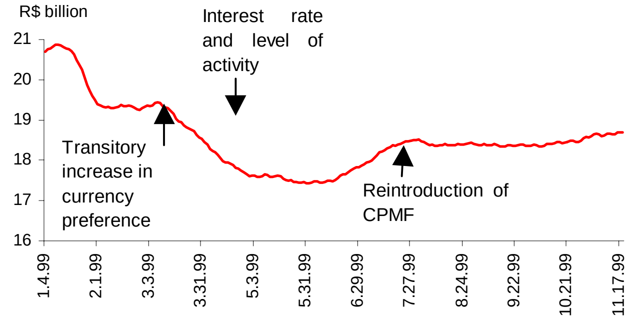
In the Banco Central methodology, the duration and average term of preset and exchange securities correspond to Macaulay's concept of duration. In the case of papers indexed to interest rates, Macaulay's concept remains valid as an average redemption term, but does not express price sensitivity to that rate, since a change in the rate of interest impacts the price of indexed papers only within the period remaining to the updating of the indexing factor, at which point the security incorporates a new value level. For example, duration of a security like the NTN-H, which is indexed monthly by the Reference Rate (TR), will be a maximum of 1 (one) month, while duration for papers such as LFTs will be just 1 (one) day since they are indexed to the Selic rate. Since neither of them has intermediate coupons, both NTN-H and LFT will have average terms equivalent to their redemption periods.

Practical applications for the concept of duration can be noted both in financial portfolio management and in macroeconomic policy implementation. From the point of view of financial management, if duration of the assets is equal to that of the liability, the worth of that asset will be immune to small interest rate changes. An example of speculative administration would be to adjust worth on the basis of expectations of interest rate alterations, in such a way as to valorize the asset more than the liability (or devalue it less). If the speculative manager expects interest rates to decline, one of the financial leverage instruments used is to maintain duration of the asset greater than that of the liability.

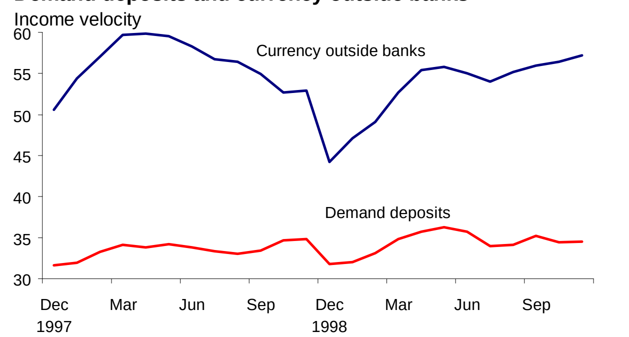
In the specific case of financial intermediation, one of its functions is to bring the cash flows of agents into alignment, making the economy's supply and demand of financing compatible. In an environment of intense concentration of instruments designed to attract short-term funding, financial institutions tend to a greater degree of mismatching in the duration of their assets and liabilities as they expand their investments in credit. To reduce their exposure to interest rate fluctuations, these institutions increase their demand for the so-called "treasury instruments", such as short-term public securities.

From the macroeconomic point of view, the increase in the presetting of the public debt, represented by growth in its duration, reinforces one of the monetary policy transmission mechanisms, denominated the "wealth channel", at the same time in which it reduces debt volatility. In other words, the greater the presetting of the debt, greater will be the impact of a change in interest rates on the financial wealth of agents. At the same time, from the point of view of public finance, greater average duration means lesser cost volatility in the securities debt, since the rolling of the debt will incorporate new interest rate levels more slowly. Consequently, the fiscal impact of monetary policy will be less accentuated.

Currency outside banks - 21 days moving average

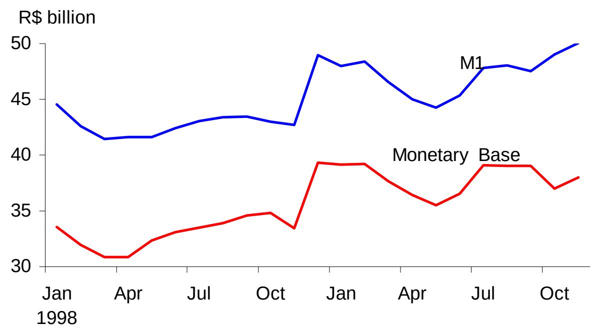


Demand deposits and currency outside banks [1/]

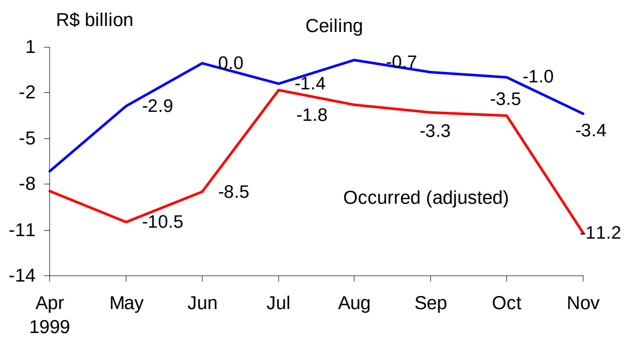


1/ Defined as the ratio between 12 month accumulated GDP (deflated by IGP-DI) and monthly average balance of the monetary aggregate.

Monetary Base and M1 - daily average balances



Net Domestic Assets



Performance criterion: April, June and September 1999.

Viewed under the prism of average daily balances, the monetary base remained stable in September. In the following month, the aggregate registered a reduction of 5.2%, as the average balance of currency issued turned in growth of 1.6% and that of banking reserves shrank by 13.1% as a result of reductions of 75% and 65% in the rate of compulsory reserves on demand deposits and deposits subject to notification. The new rate went into effect as of the start of the month. In November, the monetary base expanded by 2.6%, reflecting increased currency demand.

Expressed in the form of ceilings on net domestic assets (defined as the difference between the monetary base and net international reserves), the monetary targets negotiated with the International Monetary Fund (IMF) have been fully met. Thus, net domestic assets closed R$ 2.6 billion below the ceiling in September, a month in which the target was defined as a performance criterion in the IMF agreement. In October and November, the result was R$ 2.5 billion and R$ 7.8 billion below the target, respectively.

In the broad concept (M4), the money supply registered monthly growth of 2.1% in November and 22% in accumulated twelve month terms. Performance of this aggregate, which expanded at a pace above the rate estimated by the weighted average of the capitalization of its components, suggests a performance consistent with a process of gradual recovery in financial system credit operations.

1.4 - Investment

Gross capital formation

Production of capital goods

% accumulated growth in year

Itemization	1999				
	Jun	Jul	Aug	Sep	Oct
Industrial	-15.9	-15.4	-14.1	-12.8	-11.3
Serial	-13.9	-13.3	-12.0	-10.6	-9.0
Nonserial	-22.8	-22.5	-21.4	-20.3	-19.4
Agricultural	-18.8	-20.4	-20.6	-20.5	-19.2
Agricultural parts	-4.2	-5.8	-6.3	-6.6	-6.2
Building	-44.0	-46.0	-45.3	-44.2	-43.0
Electric energy	-12.3	-11.3	-10.6	-9.8	-78.0
Transportation	-3.8	-6.3	-6.0	-6.1	-52.0
Mixed	-10.2	-11.6	-11.0	-10.1	-10.1

Source: IBGE.

Indicators that reflect investment demand suggest a decline in the third quarter of the year, when compared to the previous quarter. In this sense, production of capital goods fell by 2.4% while that of construction inputs dropped by 0.25%, based on data purged of seasonal factors. At the same time, Ipea estimates shows that the investment rate came to 19.4% of GDP in September 1999 when one considers the last four quarters, as compared to 20.1% in June and 21.6% in September 1998.

Up to October, accumulated imports and internal capital goods output dropped by respective rates of approximately 14.9% and 11.6%, in relation to the corresponding period of the previous year. Notwithstanding 3.1% expansion in capital goods production in the month of October, following two months of relatively sluggish growth, the overall output level for the August-October quarter closed at 0.9% below the previous quarter’s level. According to Anfavea, production of farm machines declined by 15.1% up to November, while the segments of buses and trucks turned in reductions of 32% and 18.4% in that order.

The results for the construction industry, which accounts for approximately 60% of the composition of investments, indicated a slight reduction in the pace of deceleration in this sector from 4.9% in the first half to 4.6% in accumulated terms up to September, when compared to the corresponding periods of the previous year. Analyzed on the basis of seasonally adjusted data, production of inputs for the sector, which expanded by 2.6% in the month of October, turned in a reduction of 4% for the year, when seen against the results of the same 1998 period.

Mirroring the performance of investment indicators, total BNDES System (BNDES, Finame and BNDESPAR) disbursements dropped by 20.9% up to October. A sector-by-sector analysis indicates that the decline was mostly a result of cutbacks of 46% in financing to commerce and services, while operations with the manufacturing sector and crop and livestock farming increased by respective rates of 7.1% and 3.1%. Absorption of resources by the extractive industry, which accounted for 1.4% of the total disbursed, expanded by 314.8%.

The methodology for calculating long-term interest rates - the basic cost factor of BNDES resources - was altered in the final quarter of 1999. In the first nine months of the year, the rate was set on the basis of the weighted average of annual average profitability of foreign debt papers, with a minimum term of 1 year, and of the internal federal debt, with a minimum term of six months. Here, the ceiling was defined as the average of the last 12 months multiplied by a factor of 1.1. This system placed long-term interest rates at 12.84% per year in the first quarter of 1999 and 13.48% per year and 14.05% per year in the subsequent quarters. Since the month of October, the rate has been calculated on the basis of expectations of internal inflation and the country risk, as perceived by the international market. The result was a rate of 12.5% for the quarter.

Investment indicators

% accumulated growth in year

Itemization	1999			
	Jul	Aug	Sep	Oct
Production of capital goods	-13.6	-13.1	-12.5	-11.6
Inputs for the building industry	-4.9	-4.6	-4.5	-4.0
Imports of capital goods	-11.8	-10.0	-12.9	-14.9
Direct investments (except privatizations)	41.8	19.0	23.3	6.7
BNDES	-21.7	-22.7	-24.6	-24.2

Source: IBGE, SRF, BCB and BNDES

Funding inflows in the form of net direct foreign investments increased by 12.1% in the year up to November, when compared to the same period of the previous year. In terms of sector-by-sector distribution, estimates based on contracted exchange indicate a concentration of resources in the sector of services (65.4%), particularly telecommunications (25%). Industry received 18.3% of inflows, of which about 55% were channeled into chemicals and pharmaceuticals, automotive vehicles and cargo vehicles and electric equipment.

Inventories

Inventory level indicators in the various sectors of the economy point to a downturn in the third quarter. However, there is no evidence of significant short-term pressures on prices, since stocks are still relatively high. The only real exception is found under farm products, such as beans and corn, since the 1999 harvest was barely sufficient to meet internal demand.

In the opposite sense, October vehicle stocks at factory sales outlets closed at the highest level of the year. A comparison between the average stock level up to October of this year with that of the previous year shows growth of 27.1%.

The Getúlio Vargas Foundation's survey "Sondagem Conjuntural" pointed to relative stability in the stock levels of the manufacturing sector from July to October. The percentage of companies that classified their stocks as normal or excessive remained stable at 39% and 10%, respectively, while the share that considered their stocks insufficient increased from 2% to 4%.

The National Confederation of Industry's Businesspersons Industrial Confidence Index also pointed to third quarter stability in inventory levels.

1.5 - Fiscal result

The central government registered a positive primary result of R$ 1.3 billion in October, raising the accumulated surplus for the first ten months of the year to R$ 22 billion. This figure was based on a R$ 29.2 billion surplus in National Treasury accounts and deficits of R$ 6.6 billion and R$ 600 million in the social security and Banco Central accounts.

The central government surplus as a proportion of GDP increased by 0.65% in the January-October 1998 period to 2.66% in the same period of the current year. This performance is consistent with the federal government's efforts to meet the fiscal performance targets defined for the consolidated public sector.

Revenues accumulated in the fiscal year totaled R$ 170.8 billion, for nominal growth of 14.4% when compared to the same 1998 period. The revenue increase is explained basically by growth in the Cofins rate; payments of debts in arrears in the areas of PIS/Pasep, Cofins and the corporate income tax; and incorporation of judicial deposits into the single account, effective as of December 1998.

Expenditures accumulated in the period added up to R$ 148.2 billion or 17.9% of GDP. This figure represents nominal growth of 3% in relation to outlays in the same 1998 period, when the total came to 19.1%. Expenditures under the responsibility of the federal administration (personnel and charges and current and capital spending) declined by 4.2% to a level of 51% of total outlays. At the same time, transfers to states and municipalities and coverage of social security benefits registered nominal growth of 16% and 9.7%, respectively.

The federal tax inflow, for which the Secretariat of Federal Revenue is responsible, came to R$ 123.4 billion in the January-October period, for nominal growth of 9.7% in relation to the same 1998 period. Inflows in the two periods remained at the same level of R$ 130.4 billion when updated at October/99 prices by the general price index - domestic supply.

Among the different taxes, those that registered the highest nominal rates of growth were Cofins (64.1%), the financial operations tax (IOF) (41.9%); contributions to PIS/Pasep (33.4%), the import tax (18.1%) and the income tax (11.2%). Payments of debts in arrears made a significant contribution to PIS/Pasep and Cofins inflows, at the same time in which the increase in the rate of these contributions and their extension to financial institutions also contributed to the revenue increase. The IOF inflow resulted from a rate increase in the period from January to July and levying of this tax on funding channeled to investment funds. To some extent, the increase under this heading contributed to partially offsetting the revenue loss generated by the delay in charging of the CPMF.

In the opposite sense, revenues earned on inflows of the industrialized products tax fell by 2.3%, while the social contribution on profits declined by 3.1% and the inflow through the CPMF diminished by 21.1%. In the case of the CPMF, one should note that this comparison involves ten months of inflow in 1998 and approximately six months in the current fiscal year.

Public sector borrowing requirements

In terms of fiscal performance, 1999 has been a turning point, marked by record primary surpluses and real interest rates well below those of the preceding year.

Several different bills are now before the Congress and are designed to ensure the continuity of the fiscal adjustment process by creating the conditions required for a structural adjustment of the nation's public accounts. Among these, one should mention the Fiscal Liability Act and enabling legislation on the Administrative, Tax and Social Security reforms.

The monthly nonfinancial public sector primary result registered a surplus in the first ten months of the year. The accumulated surplus in the January-October period reached R$ 32 billion, as compared to R$ 2.2 billion in the same period of the previous year. This result was R$ 6.8 billion above the fiscal performance criterion agreed upon with the IMF for the period and brought the year's result to a level R$ 1.8 billion above the minimum level defined for the year.

An analysis by government spheres shows that the central government, which includes the federal government, Banco Central and Social Security System, turned in a surplus of R$ 23.6 billion, state governments closed with R$ 1.8 billion, municipal governments with R$ 1.2 billion and state companies with R$ 5.3 billion.

In the first ten months of the year, total nominal interest appropriated on an accrual basis came to R$ 123.9 billion, as compared to R$ 58.6 billion in the same period of the previous year. This expansion was, to a great extent, a reflection of the January 1999 exchange devaluation. Evidence of this is found in the fact that, were this impact on the indexed securities debt to be excluded, total interest appropriated up to October would come to R$ 68.3 billion, as against R$ 55.2 billion in the same 1998 period.

An analysis of the distribution of total nominal interest shows that, of the R$ 123.9 billion appropriated up to October, R$ 93.7 billion or 75.6% refer to the central government (federal government and Banco

Central do Brasil) and R$ 25.3 billion (20.4%) to the states and municipalities, while the remainder represented state company liabilities.

Consequently, up to the month of October, the nominal result was a deficit of R$ 84 billion, or 11.5% of GDP.

Total real interest, defined as the difference between nominal interest and monetary indexing, came to 9.1% of GDP up to October, as compared to 7.7% of GDP in the same period of 1998. The increase in real interest in the year can be ascribed to exchange devaluation, since the Selic interest rate deflated by the IGP-DI dropped substantially, moving from 26.3% per year to 6.6% per year. The impact of devaluation becomes explicit when real interest is broken down by public sector sphere, since the federal government and federal government companies, which are the most heavily exposed to exchange variations, closed with increases, while the other spheres registered downturns in the real interest burden.

Despite growth in real interest, the public sector operational result has evolved positively. In this sense, an analysis of the January-October 1999 period shows an operational deficit of R$ 40.1 billion (5.3% of GDP), compared to R$ 55.8 billion (7.4% of GDP) in the same period of 1998. The outlook for the year as a whole reflects a scenario in which interest rate reductions and relative exchange rate stability will aid in maintaining the ongoing reduction in public sector borrowing requirements.

Net debt

In October, the net public sector debt reached a level of R$ 519.1 billion (48.8% of GDP), as compared to R$ 385.9 billion (42.4% of GDP) at the end of 1998. The federal government and Banco Central accounted for R$ 321.6 billion of the debt (30.3% of GDP), while states and municipalities were responsible for R$ 165.7 billion (15.6% of GDP) and state companies for R$ 31.7 billion (3% of GDP).

For the most part, growth in the total net debt by 6.4% of GDP is a consequence of alterations in exchange. However, even with this, the

Projects awaiting congressional approval
Position on 12.16.99

1 - Fiscal Liability Law

- legal instrument: complementary law (PLP no, 18/99), defines the fundamental principles of responsible fiscal management and general norms to guide administration of public resources;
- current voting status at Congress: rapporteur's report to be voted at the Special Committee of the Chamber of Deputies.

2 - Administrative Reform regulations

- legal instrument: ordinary legislation (PL-4,811/98) that disciplines the system of public sector employment of personnel belonging to the direct administration, semi-autonomous agencies and foundations;
- current voting status at Congress: approved at the Chamber of Deputies on 8.11.99 and sent to the Federal Senate.
- legal instrument: complementary legislation (PLP 248/98), regulates the loss of public positions as a result of insufficient performance on the part of civil servants with job stability;
- current voting status at Congress: approved at the Chamber of Deputies on 8.17.99 and sent to the Federal Senate.
- legal instrument: constitutional amendment (PEC 137/99), defines limits on wages in the three levels of government;
- current voting status at Congress: approved at the Constitution and Justice Committee of the Chamber of Deputies on 11.3.99. The Special Committee was formed on 11.18.99 with the task of discussing the substantive aspects of the bill.

3 - Tax Reform

- legal instrument: constitutional amendment (PEC 175/95).
- current voting status at Congress: the rapporteur's report was approved at the Special Committee of the Chamber of Deputies on 11.23.99, with specific points that were set aside to be voted separately.

4 - Regulation of the Social Security Reform

4.1 - Relationship between the federal government, states and municipalities and their closed institutions of complementary social security

- legal instrument: complementary law (PLP 8/990);
- current voting status at Congress: awaiting rapporteur's report at the Constitution and Justice Committee.

4.2 - Complementary private social security regime

- legal instrument: complementary law (PLP 10/99);
- current voting status at Congress: awaiting rapporteur's report at the Constitution and Justice Committee.

4.3 - General rules regulating the establishment of the complementary social security regime by the federal government, the states, the Federal District and the municipalities

- legal instrument: complementary law (PLP 9/99);
- current voting status at Congress: awaiting rapporteur's report at the Constitution and Justice Committee.

4.4 - Social security contribution of the military and retired employees

- legal instrument: constitutional amendment (PEC 136/99);
- current voting status at Congress: acceptability has been approved at the Constitution and Justice Committee of the Chamber of Deputies on 11.10.99. The Special Committee was formed on 11.18.99 with the task of discussing the substantive aspects of the bill.

rise was lower than in 1998 (7.8%). Based on the concept of the net fiscal debt, which demonstrates the effect of borrowing requirements on the debt stock, since it excludes the effect of asset adjustments, including the methodological adjustment of the foreign debt and the privatization adjustment, growth came to 2.7% of GDP up to October, well below the preceding year’s rise of 7.2% of GDP.

When the impact of the exchange devaluation on the securities debt indexed to the rate of exchange is excluded, the net fiscal debt turned in a reduction of 1.9% of GDP in the first ten months of the year. This result is a clear indication of the effectiveness of the fiscal adjustment implemented in the course of the year.

1.6 - Balance of goods and non-factor services

In the second half up to November, demand for goods and non-factor services maintained the trajectory that had marked the first half of the year. This result contributed to a reduction of the deficit to US$ 5.8 billion between January and November, as compared to a deficit of US$ 13.4 billion in the corresponding period of 1998.

Trade balance

Goods and non-factor services

US$ billion

Itemization	1998	1999					
		I Q	II Q	III Q	Oct	Nov	Jan-Nov
Goods and services	-14.6	-1.7	-1.0	-1.5	-0.6	-1.0	-5.8
Trade balance	-6.6	-0.8	0.2	-0.2	-0.2	-0.5	-1.5
Non-factor services	-8.0	-0.9	-1.2	-1.3	-0.4	-0.4	-4.3

Following a US$ 4.4 billion total in May, export revenues fluctuated between US$ 4.1 billion and US$ 4.3 billion in the months from June to November. This performance reflects the slow process of recovery in the prices of some of the nation's major export products, coupled with declines in the economic activity levels of major trading partners. In relation to the previous year, however, the accumulated drop has diminished and closed November at a level of 8.1%, thus indicating a gradual recovery in the total revenue.

Trade balance - FOB

US$ million

Period		Exports	Imports	Balance	Trade flow
Nov	1999	4 002	4 531	- 529	8 533
	1998	3 702	4 727	-1 025	8 429
% change		8.1	-4.1		1.2
Jan-Nov	1999	43 333	44 789	-1 456	88 122
	1998	47 176	53 276	-6 100	100 452
% change		-8.1	-15.9		-12.3

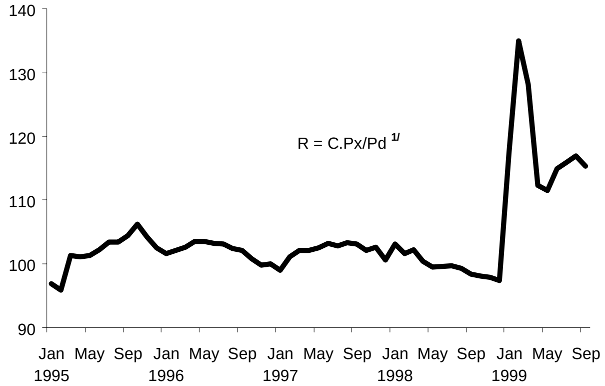
Source: MDIC/Secex

In November, imports totaled US$ 4.5 billion, or just about the same amount as in June, August and October. This relative stability is a consequence of evolution under activity levels in the course of the year when the falloff in foreign purchases was less intense than had been expected at the time of the January exchange devaluation.

In this framework, the trade balance turned in a negative result of US$ 154 million in October and a deficit of US$ 529 million in November, raising the accumulated deficit for the year to US$ 1.5 billion. The November result can be ascribed to seasonal cutbacks in exports and growth in import operations, particularly foreign purchases of aircraft.

Though the overall trade flow in the period from January to November was 12.3% below the level for the same period of 1998, the accumulated trade balance deficit moved from US$ 6.6 billion in January 1999 to US$ 2 billion in November. This trajectory confirms the positive impact of structural and transitory alterations on export and import operations and indicates that a strong trade surplus can be expected in 2000.

Profitability index of exports



Source: Funcex

1/ R= Profitability index
C= dollar average rate
Px= Export price index
Pd= Cost index associated to exports total

The gains in the competitiveness of the nation's exports that resulted from devaluation of the real at the start of the year have become more evident as exchange rates have settled into a steadier course. Following an initial rise, the profitability rate on exports declined as exchange moved upward and, according to Funcex, closed at a level 16% higher than prior to the devaluation. The stabilization of the effective gain in competitiveness tends to reduce uncertainties among exporters and contribute positively to the performance of foreign sales.

Exports and imports by Economic Blocs - FOB
January-October *

US$ million

Itemization	Exports			Imports			Balance	
	1998	1999	% change	1998	1999	% change	1998	1999
Total	43 474	39 331	-9.5	48 549	40 258	-17.1	-5 075	- 927
Laia	11 427	8 393	-26.6	10 606	7 587	-28.5	821	806
Mercosul	7 580	5 470	-27.8	8 070	5 557	-31.1	- 490	- 87
Argentina	5 807	4 317	-25.7	6 889	4 819	-30.0	-1 082	- 502
Others	1 773	1 153	-35.0	1 181	738	-37.5	592	415
Others	3 847	2 923	-24.0	2 536	2 030	-20.0	1 311	893
USA 1/	8 266	8 951	8.3	11 341	9 659	-14.8	-3 075	- 708
European Union	12 563	11 393	-9.3	13 782	12 475	-9.5	-1 219	-1 082
Eastern europe 2/	1 073	877	-18.3	684	509	-25.6	389	368
Asia	4 817	4 834	0.4	6 674	5 304	-20.5	-1 857	- 470
Japan	1 899	1 838	-3.2	2 769	2 120	-23.4	- 870	- 282
Korea, Rep.	402	521	29.6	853	851	-0.2	- 451	- 330
China	824	558	-32.3	846	698	-17.5	- 22	- 140
Others	1 692	1 917	13.3	2 206	1 635	-25.9	- 514	282
Others	5 328	4 883	-8.4	5 462	4 724	-13.5	- 134	159

Source: MDIC/Secex.
1/ Includes Puerto Rico.
2/ Albania, Bulgaria, Hungary, Poland, Slovak Republic, Czech Republic, Romania and countries of the former Soviet Union.
* Preliminary

This trend should be further strengthened by renewed growth in the countries of Asia and the consequent expansion of exports to those nations in the coming months. In the January-October period, the trade deficit in operations with Asia came to US$ 470 million, as compared to a US$ 1.9 billion negative result in the same period of 1998. In the year under analysis, the negative result was based on growth of 0.4% in exports and a 20.5% cutback in imports.

Another favorable aspect is continued robust growth in the United States, as mirrored in 8.3% accumulated expansion in Brazilian exports up to October. It should be stressed that the trade flow involved such manufactured goods as aircraft, footwear and auto parts. Since import operations declined by 14.8%, the bilateral deficit came to US$ 708 million, as compared to US$ 3.1 billion in the same 1998 period. In the month of November, exports continued growing and registered expansion of 14.2% in comparison to the corresponding period of 1998.

The economic outlook in the European Union member countries has been quite promising and this should have a beneficial impact on Brazilian foreign sales. Notwithstanding this performance, the falloff in the trade deficit with that bloc from US$ 1.2 billion to US$ 1.1 billion in the period from January to October 1998 to the same 1999 period was a consequence of sharper cutbacks in imports than growth in exports. In November, exports to the bloc increased by 3.9% in comparison to the same month of the previous year.

In the opposite direction, the growth outlook for Brazilian foreign sales to the Laia countries would tend to be negatively impacted by the perspective of no significant growth in the economies involved. The reduction in foreign sales to this bloc came to 26.6% up to October, at the same time in which imports plunged by 28.5%, thus reducing the surplus from US$ 821 million in 1998 to US$ 806 million in 1999. In terms of the trade flow with the Mercosul countries, imports fell by 31.1% and exports diminished by 27.8%, mostly involving goods produced by the transportation industry. The result was a reduction in the deficit from US$ 490 million in 1998 to US$ 87 million in 1999. In the month of November, foreign sales to the region continued on a downward curve and registered an 8.5% falloff in comparison to the same period of 1998. In the case of Argentina, the cutback closed at a level of 2%.

Exports by aggregate factor - FOB

US$ million

Itemization	November *			January-November *		
	1998	1999	% change	1998	1999	% change
Primary products	792	882	11.4	12 129	10 868	-10.4
Industrial products	2 861	3 028	5.8	34 429	31 681	-8.0
Semimanufactured	593	663	11.8	7 448	7 113	-4.5
Manufactured	2 268	2 365	4.3	26 981	24 568	-8.9
Special operations	49	92	87.8	618	784	26.9
Total	3 702	4 002	8.1	47 176	43 333	-8.1

Source: MDIC/Secex
* Preliminary

An analysis of foreign sales by aggregate factor indicates that revenues have recovered in all categories. A comparison between October 1999 and the same month of 1998 points to quantum growth in these operations, since prices remained below the level of October of last year, despite a small recovery in the last months. In relation to the same month of the previous year, this upward revenue movement continued in November.

From January to November, foreign sales of basic products declined by 10.4% and closed at US$ 10.9 billion. The listing of the products with the sharpest declines includes some of the nation's major export products, such as soybeans (-US$ 594 million), iron ore (-US$ 492 million),

Imports by category of products - FOB

US$ million

Itemization	November *			January-November *		
	1998	1999	% change	1998	1999	% change
Consumer goods	883	664	-24.8	9 824	6 692	-31.9
Durable	424	273	-35.6	4 836	2 888	-40.3
Nondurable	459	391	-14.8	4 988	3 804	-23.7
Raw materials	2 087	2 262	8.4	24 922	21 963	-11.9
Fuels	256	425	66.0	3 906	3 789	-3.0
Capital goods	1 501	1 180	-21.4	14 624	12 345	-15.6
Total	4 727	4 531	-4.1	53 276	44 789	-15.9

Source: MDIC/Secex
* Preliminary

soymeal (-US$ 306 million) and tobacco in leaf (-US$ 72 million). On the other hand, foreign sales of chicken meat (16.8%) and beef (58.1%) closed with highly positive expansion.

Semimanufactured products registered more accentuated declines under prices (17.6%) and growth in the volume of exports (14.3%), for an overall revenue reduction of 5.9% to a level of US$ 6.5 billion in 1999. When one looks at November exports, revenues accumulated in the year came to US$ 7.1 billion. Here, one should note that, in accumulated January to November terms, sales of semimanufactured iron and steel goods dropped by 18.8% while sales of cellulose moved sharply upward by 18.1% when viewed against the same period of 1998.

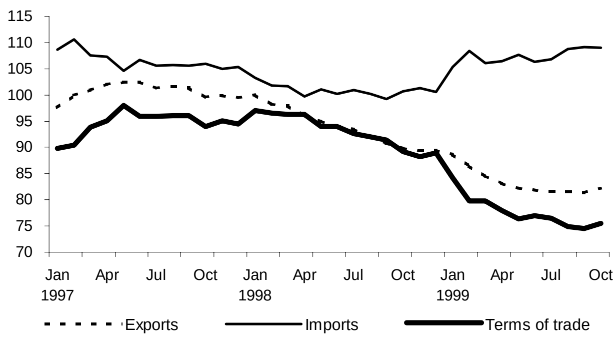
Manufactured goods accounted for 56.7% of foreign sales in the January-November period and registered revenues that were 8.9% below the 1998 level. Special mention should be given to aircraft, whose total sales of US$ 1.7 billion represented the third most important item among Brazilian exports. These sales were higher than soybean exports and represented expansion of 57.8% in relation to 1998.

An assessment of the import segment by product category indicates declines in all groupings when one compares November 1999 results with those of the same month in 1998. Imports of consumer durables and nondurables closed with the largest relative decline (31.9%). This falloff was strongest under consumer durables (40.3%), which could be sign of a process of import substitution generated by the change in relative prices that occurred in the wake of the exchange devaluation. Automotive vehicles was the heading most responsible for the performance of this category, with a falloff of 34.8% in imports, which came to US$ 997 million.

Foreign purchases of raw materials fell by 11.9% up to November and closed at US$ 22 billion, accounting for 49% of overall operations as against 47% in 1998. Up to October, prices expanded by 4.7% in relation to the previous year, establishing a trend that is expected to be further stimulated by recovery in the Asian economies. Among the products that registered import reductions, particular mention should be made of commodities, as in the case of non-food farm products with a reduction of 24% and primary food products with a falloff of 22% up to October.

Imports of capital goods diminished by 15.6% and closed with an accumulated total of US$ 12.3 billion up to November. This movement reflects a downward trajectory in the volume of imports at the same time that prices increased. This is evident in data available up to October, with respective variations of -27.3% and 13.2%. Substitution of these imports is expected to begin with products of less technological complexity and generate important impacts on next year's foreign purchases. To some extent, this process will offset the growth expected as a result of Brazilian economic expansion in 2000.

Growth in price and terms of trade indices



In the month of October, the terms of trade index (seasonally adjusted) reversed the downturn that began in January 1998, reflecting the deceleration in export prices drop that dates back to March and the positive growth attained in October, in a context of relative stability in import prices.

Though it has not yet made the new price relation perceived by economic agents fully explicit, the trade balance, in general lines, has shown signs of revenue growth brought about, to some extent, by higher prices for some of the nation's major export products and more intensive demand in the countries of Asia, the European Union and the United States.

Services

In the January-November period, the net flow of services unrelated to production factors remained at a level below that of the previous year. In this context, international travel accumulated net outlays equivalent to one third of those registered in the same 1998 period. This result was sharply impacted by increases in travel costs for residents, while outlays on transportation and diverse services fell by respective rates of US$ 473 million and US$ 195 million.

Services

Itemization	1998	1999					
		I Q	II Q	III Q	Oct	Nov	Jan-Nov
Total	-28.8	-5.0	-7.7	-4.9	-2.4	-1.8	-21.8
Interests	-11.9	-2.9	-4.8	-2.5	-2.3	-1.1	-13.6
Profits and dividends	-7.2	-1.2	-1.1	-0.9	0.3	-0.2	-3.0
Transportation	-3.3	-0.6	-0.7	-0.7	-0.2	-0.3	-2.5
International travel	-4.1	-0.2	-0.3	-0.5	-0.1	-0.1	-1.3
Sundry	-1.8	-0.1	-0.5	-0.2	0.0	-0.1	-0.9
Other	-0.4	-0.1	-0.2	-0.1	-0.1	0.0	-0.5

US$ billion

Net payments of services related to production factors up to the month of November declined by 4%. This movement is explained by the US$ 3.3 billion drop in net remittances of profits and dividends, which had registered net revenues in the two month period September-October of this year.

Diverse services related to production factors continued registering net outlays lower than those of the previous year. The reduction up to November came to 37.8%, with cutbacks of 67.2% in net outlays on patents and 23.6% in spending on technologies.

Up to November, accumulated interest net outlays increased by 31.1% as compared to the same period of last year. This growth reflects a US$ 1.7 billion drop in revenues and a US$ 1.5 billion increase in payments.

1.7 - Conclusion

Based on data up to the end of the third quarter or, in some cases, up to October, consumption and investment indicators do not yet indicate consistent recovery in demand. Consequently, these figures do not confirm expectations of more accentuated growth in the period, as predicted toward the end of the first half of the year.

Though most indicators closed at levels below those of the same 1998 period, changes could occur in this area in the fourth quarter of the year as a result of a more favorable outlook for the final months of 1999, as indicated by specifically targeted consumer and business surveys. One should further consider the fact that the basis of comparison has been greatly depressed as of October due to the impact of the Russian crisis.

Just as in the case of other government policies, monetary policy has been implemented with the aim of making it possible to regain economic growth in a context of continued price stability. In this way, this policy has been oriented in the sense of defining a trajectory of basic interest rates corresponding to the levels required to avoid inflationary pressures and, at the same time, generate reduction in the lending rates of the financial system.

Parallel to the process of reducing the public sector operational deficit, the cutback in lending rates will determine a growth pattern based on private outlays. This strategy is a consequence not only of exhaustion of the development model based on public sector outlays, but principally of the policy aimed at generating increased allocative efficiency and motivating the private sector to assume its rightful share of risk. With this, it will be possible to minimize the socialization of losses generated by economic activity.

The fact of the matter is that fiscal results have been a pleasant surprise. In this framework, the consolidated public sector primary result accumulated up to Octuber came to R$ 32 billion, well beyond the target agreed upon with the International Monetary Fund for 1999. Evidently, this is a clear sign of the sense of austerity that has guided public sector accounts in 1999. In this scenario, the debt/ GDP ratio will tend toward stabilization with exhaustion of the impact of the exchange devaluation.

2 - Aggregate supply

2.1 - Farm sector

Crop farming

Crop production

1000 t

Itemization	1998	1999 [1/]	% growth 99/98
Grain production	75 178	82 429	9.65
Cotton (seed)	824	994	20.63
Rice (in husk)	7 744	11 781	52.13
Beans	2 200	2 890	31.36
Corn	29 494	32 169	9.07
Soybean	31 374	30 905	-1.49
Wheat	2 232	2 379	6.59
Others	1 310	1 311	0.08
Other crops			
Banana[2/]	532	550	3.38
Potato	2 675	2 815	5.23
Cocoa (beans)	280	207	-26.07
Coffee (beans)	3 450	3 224	-6.55
Sugar-cane	338 972	332 193	-2.00
Tobacco (in leaf)	510	622	21.96
Oranges[3/]	103 659	114 210	10.18
Cassava	19 661	20 777	5.68
Tomato	2 755	3 207	16.41
Change in real output of crop sector	0.5	...	...

Source: IBGE
1/ It refers to the October Systematic Survey on Agricultural Production (LSPA).
2/ Millions of bunches.
3/ Millions of fruits.

According to IBGE's Systematic Survey on Agricultural Production (LSPA) for the month of October, total output of grain, legumes and oil-bearing crops came to 82.4 million tons, or 9.6% more than the 1998 harvest. In the southeast, south and central-west regions, which account for 90% of production, the harvest expanded by 6.93%. In the north and northeast regions, growth closed at 44.9%. The only grouping for which data are not yet available refers to winter crops in the south of the country (wheat, oats, barley and rye). These crops were still being harvested when the survey was concluded. One should note that, even with the sharp increase in grain production, the level of supply was still not sufficient to avoid pressures on prices, a situation that, to a great extent, can be attributed to low internal stocks and increased foreign sales.

The first survey of farmers' planting intentions for the next grain harvest covers nine products in the central-south region and the State of Rondônia and indicates a cutback of 0.42% in area planted or to be planted, as compared to the area utilized in the previous harvest. The major falloffs are expected to occur under rice (4%), the first bean harvest (5.7%) and the first corn harvest (1.4%). The first two of these products are items of importance to formation of the prices of what is termed the basic food basket, a listing of the fundamental staples of the Brazilian diet, while the third product is an essential ingredient of animal feed. In the case of soybeans, the estimated area to be planted will increase by 1.2% in relation to the 1998 area, while the area planted in herbaceous cotton is expected to increase by 0.6%.

Livestock

Livestock production has evolved positively in 1999, accumulating growth of 5.8% up to the third quarter of the year, according to IBGE calculations. This performance reflects growth in exports during the period, stimulated principally by the exchange devaluation at the start of the year. In this context, foreign sales of beef and poultry increased by respective rates of 73% and 24.5% up to October, when compared to those of the same 1998 period, while exports of pork declined by 4.8%. Growth in foreign sales intensified the unfavorable seasonal effects on domestic prices. Despite this, the normalization of supply together with the sustainability in the sector's pace of growth will contribute to reduce livestock prices in the coming months.

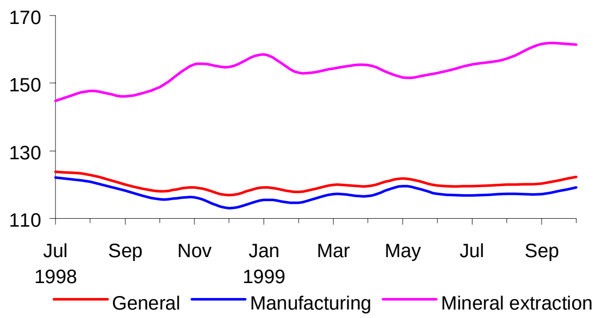
2.2 - Industry

Industrial output

Industrial output showed signs of recovery in the second half of the year. The average level of the different indices in the July to October period was 0.8% higher than in the first half of the year, based on figures drawn from the seasonally adjusted series. A breakdown by use categories indicates that this trend was backed mostly by growth of 7.5% under production of consumer durables and 1.9% in the output of intermediate goods. Production of capital goods fell by 2.8% as a result of reductions under farm machines and capital goods for the building industry, while consumer nondurables dropped by 1.8%.

An analysis of short-term industrial output performance indicates growth of 1.6% in October in the seasonally adjusted series. For the most part, this figure is based on an increase of 1.7% in the manufacturing industry and a drop of 0.2% in mineral extraction. A breakdown by category of usage shows that recovery has been generalized, though it has taken hold with greater intensity in the segments of consumer durables and capital goods, which registered respective growth rates of 4.2% and 3.1%. Output of intermediate goods and consumer nondurables and semidurables expanded by 2.1% and 0.4% in the same order. Sixteen of the twenty segments surveyed registered positive output growth, led by transportation equipment and perfume products, both of which closed with 6.9% expansion, followed by rubber (6.1%), mechanics (4.5%) and paper and cardboard (4.4%).

Industrial production
(Seasonally adjusted series)
1992=100

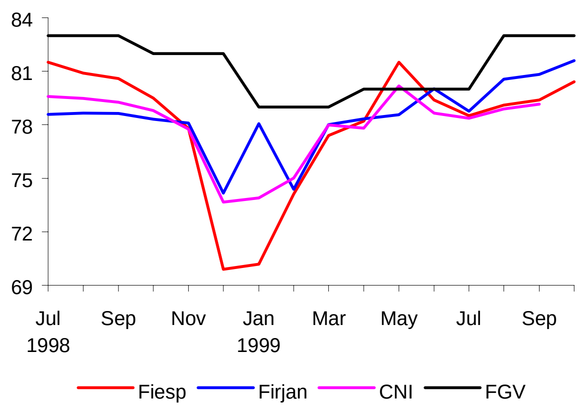


Source: IBGE

In comparison to the same 1998 period, industrial production performance up to October turned in a decline of 2.1% for industry in general with a falloff in twelve of the segments surveyed. These reductions were sharpest under electric and communications equipment (12.6%), mechanics (10.2%), plastics (7%) and metallurgy (5.1%). Among the seven segments that turned in positive growth, the most important were mineral extraction (10.1%), perfumes, soaps and candles (6%), wood (5.9%) and paper and cardboard (4.3%). An analysis on the basis of use categories shows growth of 0.5% under intermediate goods and declines of 12.5% for consumer durables, of 11.6% for capital goods, and of 2% for consumer nondurables and semidurables.

Utilization of installed capacity

Utilization of installed capacity
Average percentage



In the manufacturing industry, a Getúlio Vargas Foundation survey shows that the level of utilization of installed capacity increased from 80% in the month of July to 83% in October. In the same month of the previous year, the result had been 82%. Of the twenty-one segments surveyed, thirteen registered growth in the utilization of their production facilitates, while two closed with stability and five ended the period with declines. One should note that, in the segments of pulp, paper, cardboard and rubber, the utilization rate passed the mark of 90%. On a sector-by-sector basis, growth was across-the-board, the highest rates being registered by capital goods (from 75% to 80%) and consumer goods (from 75% to 78%).

According to the National Confederation of Industry (CNI), average utilization of installed capacity in Brazil came to 79.2% in September, compared to 78.7% in June. In the manufacturing industry in the State of São Paulo, a survey carried out by the Federation of Industries of the State of São Paulo (Fiesp) indicated growth from 79.4% at the end of the second quarter of the year to 80.4% in October.

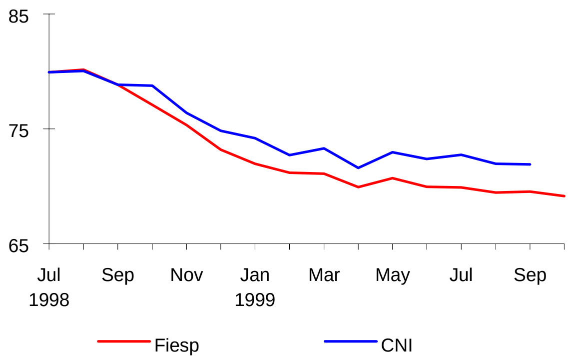
Automotive vehicle production

Termination of the Emergency Automotive Sector Agreement on September 30 had a powerful impact on vehicle production in August and September, when the total surpassed the mark of 133 thousand units, the highest in all of 1999. The segment that drew the greatest benefit from the agreement, passenger cars and light commercial vehicles, turned in growth of 11% in August, when compared to July, and closed with output of 127 thousand units. The month of September repeated this performance. The overall decline in production during the year dropped from 22.7% up to September to 17.3% up to November. The reasons underlying this performance were the small base of comparison represented by the final quarter of 1998. When one considers the series purged of seasonal factors, output in October and November expanded by 0.16% and 2.3%, respectively.

2.3 - Labor market

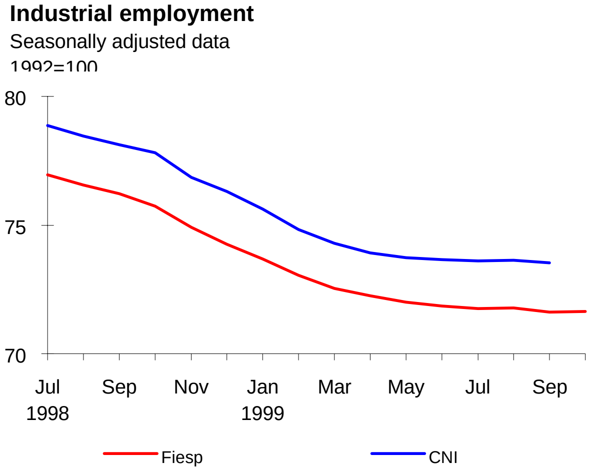
Employment

Hours worked in production
Seasonally adjusted data
1992=100



The job market has remained relatively stable with no important alterations in either open unemployment or formal employment levels. In the industrial sector, layoffs have continued at a pace greater than the creation of jobs and productivity gains have been positive, as evident in the larger decline under hours worked in comparison to the reduction in industrial sales.

In the case of the manufacturing sector, job levels have continued on a downward curve, as evident in the



monthly Fiesp survey. According to this study, data from which seasonal factors have been removed reveal that the average result of the different employment indices between July and October came to a level that was 1.19% lower than in the second quarter of the year. In the context of the CNI survey, the ratio declined by 0.25% between the third and second quarters. The comparison between the averages for the January-October 1998 and 1999 periods points to a decline of 6.63% in the Fiesp indicator, or just about the same result as shown by the CNI survey of average indices between the January to September periods of 1999 and 1998 (6.73%). In the same periods of reference, reductions also occurred in the number of hours worked and in industrial sales: 13.26% and 2.16% in the Fiesp framework and 10.42% and 1.48% in the CNI framework, respectively.

Open unemployment calculated by the IBGE in six metropolitan regions came to 7.53% in October, as compared to 7.37% in September. The average for this year closed at 7.71%, as compared to 7.78% in the same period of 1998. In terms of regional distribution in the month of October, the only reductions occurred in Recife and Salvador, while the index calculated on a sector-by-sector basis showed across-the-board expansion.

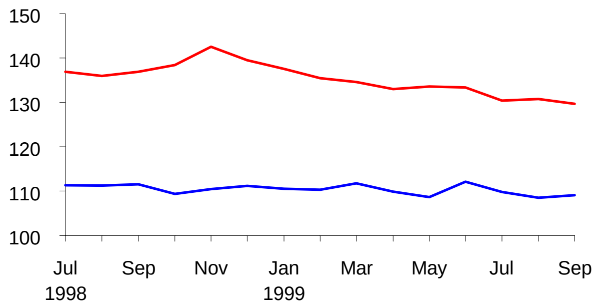
The October rise in open unemployment reflects growth in the economically active population (0.59%) that was greater than expansion of the employed population (0.41%). Consequently, despite creation of 246 thousand job positions in the last three months, this was not sufficient to absorb the growth in the economically active population. Here, one should note that the total number of persons working in October of this year came to 16.6 million, for growth of 0.43% over the same month of 1998.

In comparison to the previous month, the employment level in October increased in all segments of activity except services, where the result indicated stability. The most accentuated increase occurred under commerce (1.63%), followed by construction (1.29%) and manufacturing (0.12%). Of the total number of persons occupied, 54.4% were allocated to the service sector, 16.3% to industry and 15% to commerce. In terms of worker classifications, the number of workers without signed working papers increased by 2.5%, while the grouping of the self-employed dropped by 0.6% and the category of registered workers fell by 0.15%. In the six metropolitan regions covered by the survey, these results indicate a continued shift to the informal labor market, despite the fact that the largest share of workers is still concentrated in the formal job market (44.4%), followed by unregistered workers with 26.8% and the self-employed with 23.5%.

According to Ministry of Labor data, formal employment levels have been relatively stable during the course of the year, with growth of 0.29% up to October, reflecting creation of 63.2 thousand jobs. This total resulted from generation of 85.2 thousand jobs in the manufacturing sector, 58 thousand in the service sector and 7.1 thousand in other sectors, coupled with reductions of 67.9 thousand jobs in the construction industry and 14.3 thousand in public utility industrial services and 5 thousand in the sector of commerce. The seasonally adjusted statistical series points to expansion of 0.02% in October, with generation of 17.4 thousand jobs.

Wages and earnings

Real average earnings
(Seasonally adjusted data)
1992=100



Source: IBGE

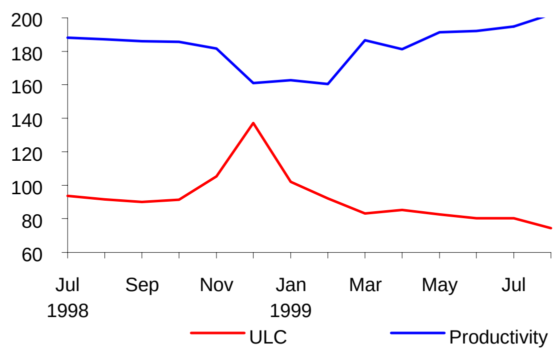
In the third quarter of the year, the behavior of wages and salaries suggests a continued decline in purchasing power, according to IBGE data. In the industrial sector, the evolution of earnings indicators, productivity and unit labor cost confirms the absence of price pressures generated by the labor market.

The IBGE household survey in six metropolitan regions indicates that average nominal and real earnings dropped by respective rates of 0.52% and 4.62% up to September, when compared to the same period of 1998. An analysis by professional category indicates that unregistered and registered workers obtained nominal gains of 3.8% and 0.48% in the period, respectively, while the largest losses occurred under employers (8.07%), followed by the self-employed (3.32%). When one analyzes the various sectors of activities, negative performances were most common, as earnings in the sector of commerce dropped by 3.42%, while those of the construction industry declined by 2.65% and the manufacturing sector closed with a negative rate of 2.48%. In contrast, the service sector remained stable. When all the different sectors are taken together, the drop in real earnings in the third quarter of the year, in comparison to the second, came to 2.25% based on seasonally adjusted data.

Specific surveys on the behavior of overall wages in the manufacturing sector carried out by Fiesp and CNI indicate a 6.62% falloff in São Paulo up to the month of October and a 9.66% average reduction up to September in the 12 states covered by the CNI survey. When one compares the average July to October index with that of the first six months of the year, based on seasonally adjusted data, one perceives the loss in the purchasing power of labor in São Paulo industry, with drops of 0.3% in real wages and 1.12% in real overall salaries. In the states analyzed by the CNI, a comparison between the third and second quarters of the year indicates stability in total real wages paid by the industrial sector.

Unit labor cost and productivity

Unit labor cost (ULC)
1992=100



Source: IBGE and BCB

Calculated as the ratio between payroll in the industrial sector, deflated by the IPA-PI calculated by the Getúlio Vargas Foundation and the industrial production index, the unit labor cost dropped by 6.35% when one compares the January-August 1999 period with the same period of 1998. This result is based on a 9.17% reduction in the payroll, a falloff that was considerably more accentuated than the decline under industrial product (3.01%).

A comparison of unit labor cost with the evolution of the productivity of labor in the industrial sector, understood as the ratio between physical production and total hours worked in production, leads to the conclusion that the labor factor made a positive contribution to the absence of price pressures. The average increase in industrial productivity came to 6.73% up to August.

In five industrial segments: mineral extraction, wood, tobacco, beverages and textiles, productivity gains surpassed the mark of 10%, while negative results were registered in only two (leather and hides and electric and communications equipment). The average for the manufacturing sector came to 5.4%.

Selected nonfinancial corporation indicators

In comparison to the previous period, the operational profits and total indebtedness of open capital nonfinancial corporations increased in the third quarter of the year. At the same time, based on a sampling of 221 companies distributed into 24 sectors, an Economática survey concluded that the average debt term has also lengthened.

At the same time, the profitability indicator of net worth deteriorated. This is a calculation of the ratio between net profits and net worth and reflects the narrowing of the margins in the median of the sectors analyzed. Thus, the net margin moved from positive in the second quarter to negative in the subsequent quarter. The degree of financial leverage in September turned in a significant reduction of approximately one third of the June 1999 value.

Such sectors as auto parts, toys and computers are exceptions to the reduction in the profitability of net worth. In the opposite sense, the worst performances were registered in the electric-electronic sector, transportation equipment and air transportation.

With respect to current liquidity, which indicates the degree of short-term financial maneuvering room, the best performances were registered in the sectors of telecommunications, petrochemicals and foodstuffs, while the sharpest reductions occurred under energy, cement and the mechanics industry.

2.4 - Gross domestic product

With the release of GDP results for the third quarter of the year, IBGE rectified information referring to the previous quarters with the principal alterations that occurred in the subsectors of financial institutions and public administration. Thus, the decline of 0.42% in the first half of the year was revised upward to growth of 0.19%.

In the third quarter of the year, the decline came to 0.18% of GDP when compared to the previous quarter in the seasonally adjusted series. With this, the accumulated result for the year closed in a position of stability. According to IBGE, deceleration was a consequence of growth in price indices as of the month of July and of the increase in the volatility of the rate of exchange.

In sectoral terms up to the month of September, expectations of favorable results in the crop and livestock sector were confirmed (6.1%), based on the performance of crops and animal production which increased by respective levels of 6.1% and 5.85%. Industry closed with contraction of 3.03%, led by the subsector of mineral extraction with 10.38% and public utility industrial services with 2.12%, while manufacturing and construction accumulated falloffs of 3.4% and 4.57% respectively.

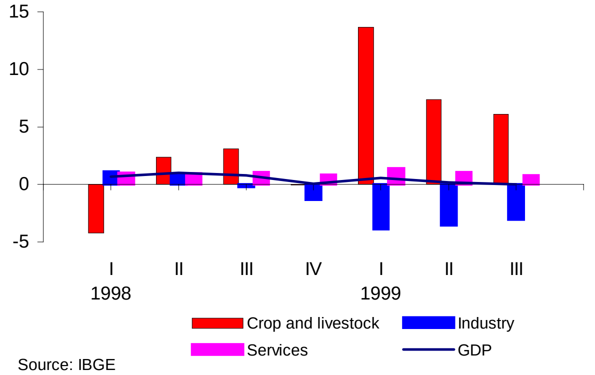
GDP - Accumulated rate in the year

Itemization	1998				1999		
	I	II	III	IV	I	II	III
GDP	0.71	1.04	0.78	0.05	0.59	0.19	0.02
Crop and livestock	-4.24	2.36	3.07	-0.02	13.64	7.36	6.10
Industry	1.15	0.87	-0.21	-1.34	-3.91	-3.57	-3.03
Services	1.03	0.97	1.05	0.83	1.39	1.10	0.80

Source: IBGE

Gross Domestic Product

% growth accumulated in the year



Source: IBGE

Insofar as services are concerned, the increase came to 0.8% or less than the figure for the first half of the year (1.1%). Deceleration was mostly a result of the negative performance of the subsector of transportation which closed with a decline of 0.38%, as against an increase of 0.39% up to June, lesser growth in communications (9.53% as compared to 13.48%), and in public administration (0.78% as against 1.09%). In the sector of commerce, the falloff came to 1.51% compared to 1.66%, registered up to June.

In comparison to the third quarter of 1998, GDP fell by 0.31% as a result of a reduction of 2.02% in production of the industrial sector. For the most part this was due to a 3.95% decline under construction and a drop of 2.23% under manufacturing. In the same period of time, the crop and livestock sector product expanded by 3.35%, powered by increases of 4.12% under crops and 2.78% under animal-based products. In the service sector, growth came to 0.22%.

2.5 - Conclusion

Industrial production declined in the third quarter of the year when compared to the second. The positive August and September results were not up to initial expectations of recovery which, consequently, were transferred to the final quarter of the year.

Insofar as the supply of crop and livestock products is concerned, the unfavorable seasonal factors of the second half of the year were accentuated by growth in foreign sales, particularly in the cases of beef and chicken.

In the labor market, no alterations occurred in the trend to stability in the second quarter of the year either in terms of formal employment or as regards the indicators based on the results of household surveys.

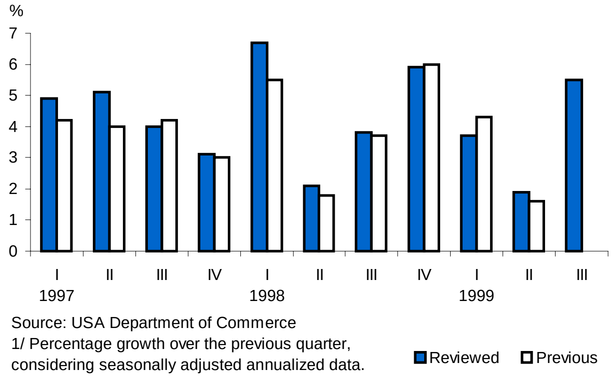
Contrary to what occurred at the end of 1997 and 1998 when production was negatively impacted by international financial crises, it is now expected that GDP will register a positive result in the final quarter of the year. According to forecasts, the final overall result for the year is expected to be near 1%.

3 - International economy

3.1 - United States

The United States economy pressed forward at an accelerated pace in the third quarter of the year. According to present indicators, this trajectory will continue into the future, albeit at a less intensive pace.

Gross Domestic Product 1/



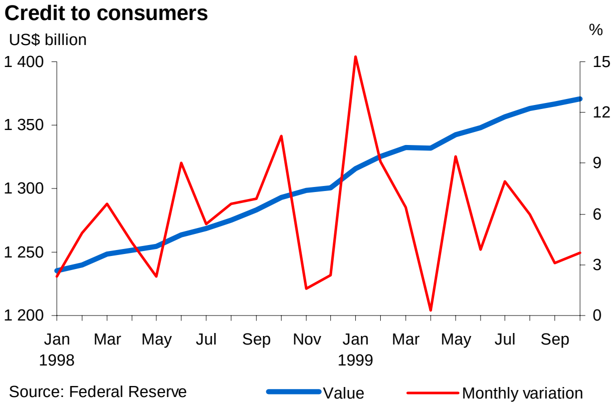
Source: USA Department of Commerce
1/ Percentage growth over the previous quarter, considering seasonally adjusted annualized data.

Release of the revised gross domestic product series showed more accentuated economic growth than originally predicted. This result had been expected since methodological alterations included outlays on software as fixed capital investments and considerable progress was achieved in measuring of services. Among other adjustments, these items contributed to raising the value of production.

Annualized GDP growth in the first three months of the year expressed in the series purged of seasonal factors, came to 3.7%, 1.9% and 5.5%, when compared to the respective preceding quarters. Growth rates in comparison to the same period of the previous year ended at 3.9%, 3.8% and 4.2%. This movement has generated estimates of product growth of approximately 4% in 1999, slightly less than the 1998 level of 4.3%.

The industrial production series, which was revised and announced in November, turned in a similar trend. In the third quarter, seasonally adjusted annualized data indicated growth of 4.8%, compared to the previous period, and was followed by growth of 0.8% in October and 0.3% in November.

The production increase has been sustained by demand which, in turn, has been strongly rooted in family absorption of production. In this context, consumer credit operations have registered successive monthly growth rates

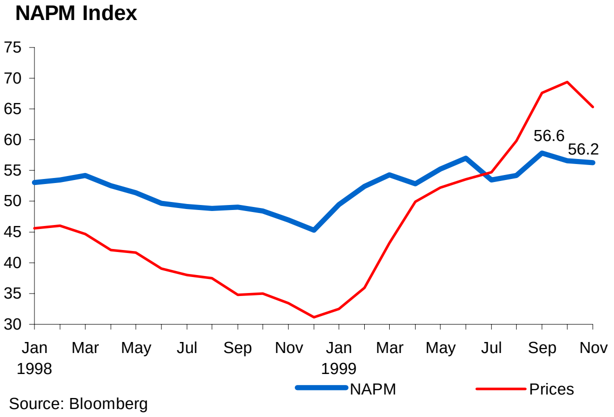


that came to 6% in August, 3.1% in September and 3.7% in October, in relation to the same period of the previous year. However, this trajectory was less accentuated in the final quarter of the year, as a consequence of a higher cost of credit.

Sales at the retail level in the month of September remained stable in comparison to the previous month, following a 1.32% growth in August (seasonally adjusted data). In October and November, sales rose by 0.32% and 0.86%, respectively. When automotive sales are excluded, the result showed growth of 0.93% in the month of August, 0.6% in September, 0.79% in October and 0.36% in November, suggesting continuity of the already robust level of demand.

The balance of trade also signaled intense economic activity. Imports of goods in the January-September period added up to US$ 748.3 billion or 10.4% more than in the same period of 1998. In the seasonally adjusted series, monthly growth points to August expansion of 2.2% and a decline of 0.14% in September. Exports of goods accumulated US$ 498.2 billion in the first nine months of the year, 0.5% more than in the same period of previous year. In monthly terms, export growth in August came to 5.8% in the series freed of seasonal impacts, followed by a 1% decline in September.

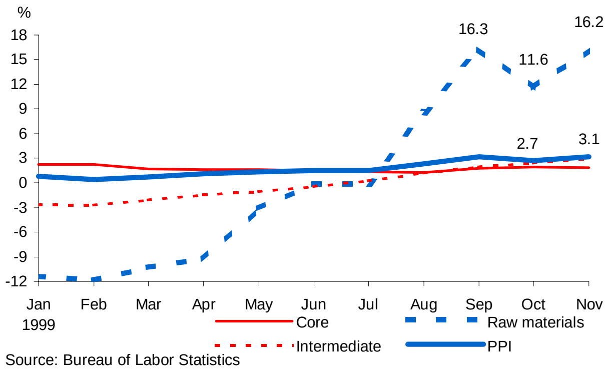
In this framework, following the record US$ 34.7 billion deficit in July, the negative balance declined slightly and came to US$ 33.6 billion in August and US$ 33.4 billion in September. When one considers the first nine months of the year, the accumulated deficit closed at US$ 250.1 billion for growth of 37.2% when compared to 1998.



The index released by the National Association of Purchase Managers points to a slight reduction in growth expectations, as the index closed October at 56.6 and November at 56.2, following an increase from 54.2% in August to 57.8 in September. However, this decline should not be interpreted as a consistent reversal in growth expectations, since the index remains above the level of 50, indicating continuation of current conditions.

The continued growth of the American economy and expectations that this process will not be interrupted in the foreseeable future demand constant monitoring aimed at avoiding undue pressures on prices, even though demand indicators and the expectations of agents would seem to point to a less accelerated growth profile.

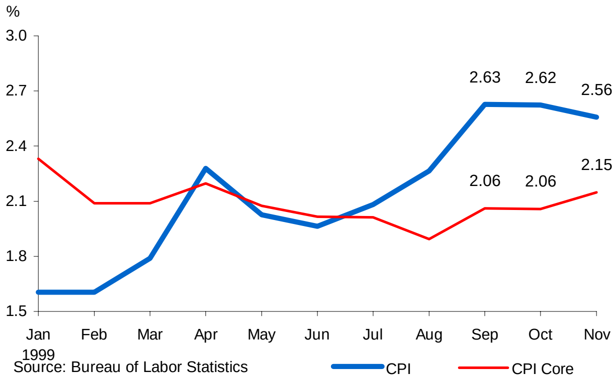
PPI - Growth accumulated in 12 months



Source: Bureau of Labor Statistics

Up to November 1999, the producer price index increased by 2.4%, as compared to 0.08% in the same period of the previous year. In accumulated 12 month terms, the index has varied during the year between 0.5% and 3.1%, with an overall upward trend. To some extent, this behavior reflects the rise in the prices of raw materials and intermediate goods, which were impacted by higher energy and commodity prices. Between January and November, the producer price index - raw materials and the producer price index - intermediate products increased by respective rates of 17.7% and 3.6%, while accumulated results for the 12 month period up to November show growth rates of 16.2% and 3%. Exclusion of food and energy prices, forming the core of the producer price index, registered a more stable trajectory during the year, with an overall variation of 0.96%.

CPI - Growth accumulated in 12 months



Source: Bureau of Labor Statistics

However, pressures on producer prices were not fully transmitted to consumers. Consequently, the consumer price index increased by 0.4% in September, 0.2% in October and 0.1% in November; its core, which excludes energy and food products, increased by 0.3%, 0.2% and 0.2%, respectively. An analysis of the 12 month accumulated index shows an upward trajectory, moving from 1.6% in January to 2.6% in November.

The evolution of the labor market and productivity was particularly relevant in this framework and may possibly signal cost pressures for the productive sector. In the month of November, the rate of unemployment continued at the level of the October record low of 4.1%. Parallel to this result, earnings per hour worked increased by 0.15%, following 0.3% expansion in the previous month.

The growth rate in the productivity of the manufacturing sector continued on the downward trajectory begun in the third quarter of 1998. Thus, in the July-September period, growth came to 3.9% in comparison to the April-June period, while the second quarter turned in growth of 5.5%. These figures are based on seasonally adjusted data and expressed in annualized terms. The unit labor cost in this sector, using the same bases of comparison, came to respective levels of 2.3% and 0.3%. In the non-farm sector, productivity in the third quarter of the year increased by 4.9%, in comparison to the second quarter, in annualized terms, while the unit labor cost declined by 0.2%.

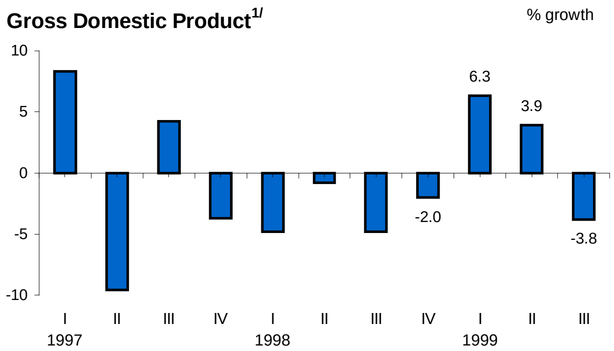
At the October 5 meeting, the Federal Reserve Open Market Committee (FOMC) evaluated the evolution of the economy as consistent with its long-term objectives of price stability and sustainable growth. The Committee resolved to hold the federal fund interest rate target at 5.25% per year. However, the Committee decided to raise the rate by 25 basis points at its November 16 meeting to 5.5% per year, even though cost pressures were considered under control. This increase was a response to the perception that the pace of growth in the activity level had surpassed the potential growth of the economy. It should be noted that, with the total increase of 50 basis points, the basic rate of the economy returned to the level in effect prior to the Asian crisis when the FOMC resolved to liberalize its monetary policy.

The response of the American economy to the interest rate rise is still considered incipient, not only in terms of the degree of the rate increase, but also in terms of the very small gap between introduction of these restrictions and the period under analysis.

3.2 - Japan

Signs of recovery are becoming increasingly more evident in the Japanese economy and, following five consecutive quarters of diminishing activity, this has been reflected in GDP growth in the final two quarters of the year. However, the foundations of this growth are still fragile. This is obvious in other economic indicators, as well as in the negative GDP growth registered in the third quarter of the year.

The GDP series and the seasonal adjustment methodology were revised. The new statistics indicate annualized growth of 6.3% in the first quarter of the year, expressed in seasonally adjusted data, when compared to the preceding quarter. In relation to the same period of the previous year, the result was a decline of 0.4% in the January to March period and a growth of 0.6% in the period from April to June.

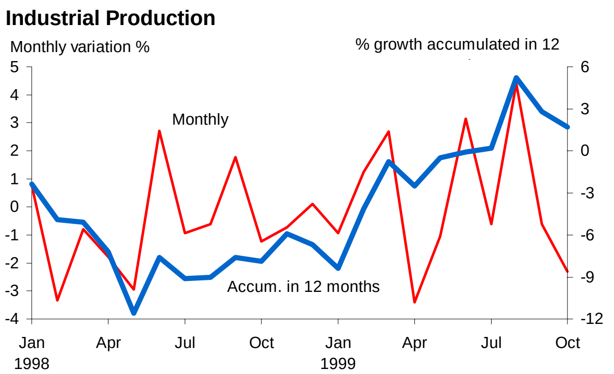


Source: Economic Planning Agency and Bloomberg
1/Growth over previous quarter, seasonally adjusted, annualized.

The preliminary result for GDP growth in the third quarter showed an annualized reduction of 3.8% in comparison to the previous quarter, expressed in data purged of seasonal factors. At the same time, these results pointed to 0.9% growth in comparison to the same 1998 period.

However, several indicators suggest an improved Japanese economic performance than that expressed in GDP data in the third quarter. In this sense, one should note that, based on seasonally adjusted data, the economic activity level index, which registered a July decline of 0.3%, turned positive in August at a rate of 1.1%, followed by a September drop of 0.8% in comparison to the respective previous months. In much the same way, the activity index for the tertiary sector, which accounts for 60% of Japanese product, remained stable in July, before rising in August (1.3%) and dropping by 0.9% in September, in comparison to the previous months. Once again, these figures are expressed in data purged of seasonal factors.

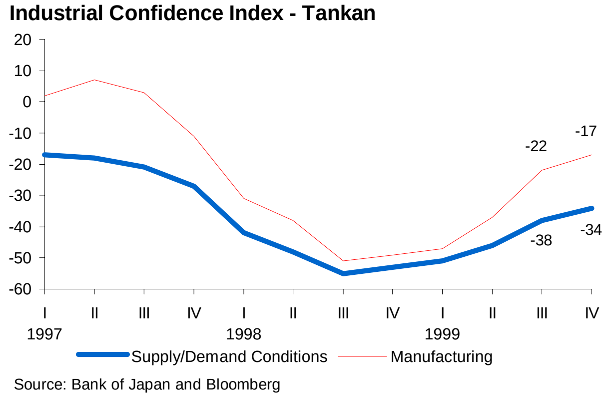
Electrical energy consumption shows a similar performance, with growth of 1.9% in August, 5.8% in September and 3.9% in October, when compared to the same months of the previous year. Industrial production fell by 0.6% in July and September, expanded by 4.4% August and fell by 2.3% in October.



Source: MITI and Bloomberg

In the first ten months of the year, the behavior of industrial production was highly volatile, accumulating a rise of 2.33%. The 12 month results showed positive growth rates only as of the month of July, a fact that had not occurred since 1998. In October, according to preliminary data, this indicator registered expansion of 1.7%.

Expectations among businesspersons with regard to the economic situation have shown favorable results

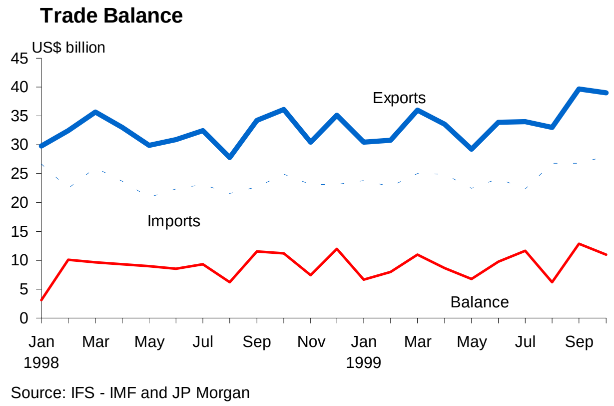


and are reflected in the most recent Tankan confidence index. Though this index closed with a negative result, improvement did occur as of the third quarter of 1998. Consequently, in the October-December 1999 period, the index shows that supply and demand conditions increased from -38 in the previous quarter to -34, while expectations regarding the performance of the manufacturing industry increased from -22 to -17.

Positive expectations with respect to the evolution of the Japanese economy led the OECD to increase its estimates of GDP growth in 1999 and 2000 by rates of 1.5% and 1.2%, respectively.

However, the analysis of aggregate demand indicators raised questions as regards the sustainability of the recovery process. Sales in the wholesale and retail sectors are still negative or registering low levels of growth in relation to the same months of 1998, closing at -6.8% and 0.2%, respectively. In October. Real family spending, which had expended by 2.6% in July, when compared to the same month of the previous year, registered declines in the months of August (1.1%) and September (3.7%).

Following four consecutive months of positive growth, housing starts declined by 0.6% in October, when compared to the same period of the previous year. However, this movement could be interpreted as a reaction to consecutive positive growth rates. Here, one should stress that the number of housing starts reached 1 million in the January-October period, 0.93% higher than in the same period of 1998.



In October, the trade balance of goods came to US$ 11 billion, based on exports of US$ 39 billion and US$ 28 billion in imports. In comparison to the same month of the previous year, exports increased by 8% and imports by 12.3%. In the year, foreign sales accumulated a total of US$ 339.7 billion, 5.4% more than in the same period of 1998, while imports totaled US$ 246.8 billion, with growth in about the same range as under foreign sales. With this, the trade balance came to US$ 92.8 billion.

This result reflects the combined impact of recovery in the Japanese economy, which tends to stimulate imports, and growth in the East Asian countries, which contributed to a favorable export performance.

Another factor that impacts the trade balance and, consequently, the performance of the Japanese economy is exchange evolution. As of July, the trend of the yen rate has been marked by successive valuations, moving from Y 122.4/US$ in the second week of July, to Y 102.67/US$, in the first week of December.

In the month of November, the Japanese government announced a series of measures aimed at stimulating the economy and, in this way, make the outlook for the future even more positive. The overall value of the program has been set at US$ 173 billion (considering the yen average rate in the month of November), 1.1% more than the amount injected into the economy through the November 1998 program. The measures that tend to generate a more direct impact on product are spending on public works and social infrastructure, which will total US$ 65 billion, corresponding to growth of 37.5% of total available funding.

The incentive instruments have received a larger volume of funding than in the previous program, particularly in the areas of assistance to small companies (US$ 70.7 billion), and investments in the housing sector (US$ 19.1 billion). Implementation of this program depends on approval of supplementary budget allocations totaling US$ 62.1 billion.

Inflation indicators do not seem to reveal any undue pressures on price levels. The consumer price index registered an increase of 0.3% in the months of August and September, following two months of negative results. In October, this index rose by 0.2%, closing the year with an accumulated fall of 0.2%. After registering 0.5% contraction in August and September, the wholesale price index increased by 0.1% in October. In November, this index closed with a decline of 0.1% raising the accumulated falloff to 1.3% in the year.

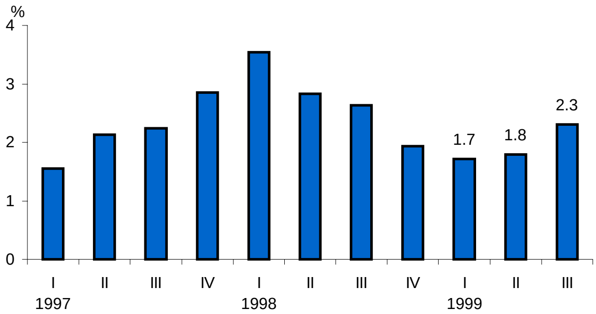
With the economy now entering a period of recovery, coupled with relative stability in inflation indices, the Bank of Japan has held the interest rate near zero. This was reaffirmed at a meeting held on November 26 and, together with other fiscal incentive measures offered by the Japanese government, has the objective of stimulating sustained growth in the Japanese economy.

Since the month of June, daily fluctuations in the interbank market interest rate have ranged between 0.03% per year and 0.015% per year. The rates for preferred clients on long-term bank loans began moving downward as of September, according to information released by the Bank of Japan. In October, these rates came to 2.2% per year, a cutback of 0.2 percentage point in relation to August.

With regard to the evolution of the rate of exchange, the Bank of Japan has intervened in the market, but without altering the valuation trajectory of the Japanese currency.

3.3 - Euro zone

Gross Domestic Product [1/]



Source: Eurostat

1/ Growth over the same quarter of previous year.

Among the euro zone member countries, the economy moved into a positive growth trajectory in 1999. Compared to the same period of the previous year, quarterly GDP growth in the 11 countries of the region came to 1.7% and 1.8% in the first and second quarters, respectively, and 2.3% in the third quarter.

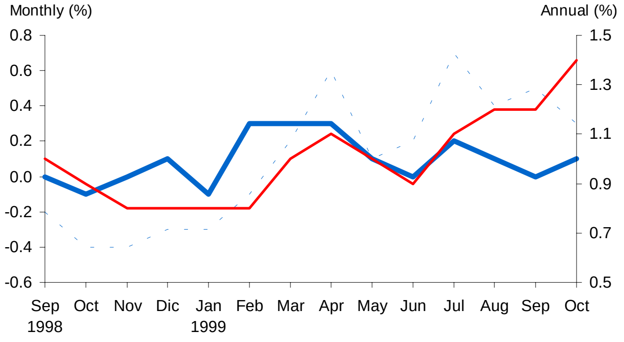
OECD projections for November indicate annual growth of 2.1% of GDP for the year, a level compatible with the growth rate interval between 2 and 2.5% that the European Central Bank considers consistent over the medium term. For the year 2000, the OECD estimates expansion of 2.3% for the region as a whole.

The evolution of industrial production generated expectations of more intense growth in the third quarter of the year. Following expansion of 2.5% in the twelve month period ended in August, industrial production indicators in the member countries of the euro zone registered growth of 0.8% in September. However, this result was negatively impacted by 0.3% contraction in Germany as a consequence of a series of shocks.

The confidence indicators among industrial businesspersons and consumers, measured by the European Commission became less negative in September and October and point to a gradual process of change in the outlook of economic agents.

In this framework of renewed growth, the European Central Bank which, in the light of expansion of the M3 monetary aggregate that it considered excessive, had already raised the basic interest rate from 2.5% to 3% on November 4, decided to maintain the rate at that level at its December 2 meeting. In the same meeting, it also decided to hold the reference rate of annual growth for the M3 monetary aggregate at 4.5%. In relation to the same month of the previous year, the increase in this variable has remained above the reference rate throughout the year and registered increases of 5.8%, 6.2% and 6%, respectively, in the months of August, September and October.

Inflation Rate

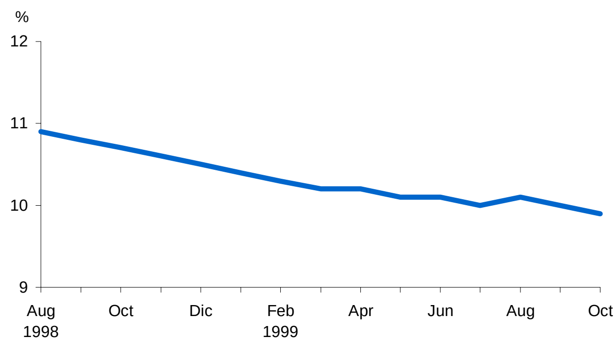


Source: Eurostat

In an environment of economic growth and low interest rates, inflation rose in the second half of the year, though it was held below 2%, a level considered consistent with price stability. Annual growth in the harmonized consumer price index, which had risen from 0.8% in January to 0.9% in June, closed the month of October at 1.4%. The performance of some of the underlying factors of inflation, such as growth in credit and liquidity, wages, producer prices and energy, suggest the possibility of upward movement in the price trajectory.

Producer price index registered increases of 1.3% in September and 2% in October, following negative annualized growth rates during the entire first six months of the year.

Unemployment Rate



Source: Eurostat

The employment level registered positive growth during the entire year as unemployment in the 11 nations moved slowly but persistently downward, closing October at 9.9% in contrast to 10.8% in the same month of the previous year.

Simultaneously to the decline in unemployment rates, the unit cost of labor registered annual growth of more than 2% in the first two quarters of the year.

Powered by devaluation of the euro against the dollar, which totaled 14% in the year up to November, the foreign sector registered trade balance surpluses. In the second quarter of the year, the positive trade balance result came to E 17.5 billion.

Germany

In Germany, GDP expanded at an annualized rate of 2.9% in the third quarter of the year, expressed in seasonally adjusted data, when compared to the preceding quarter, following expansion of 2.5% and 0.5% in the first two quarters of the year. This growth was leveraged by an 11.7% increase in exports, at the same time in which fixed investments and public and private consumption also moved upward by respective rates of 3.4%, 2.7% and 2.5%, in annual terms when compared to the previous quarter. These figures are expressed in data from which seasonal factors have been eliminated,.

Once again, utilizing data purged of seasonal impacts, industrial production, which had grown by 1.1% in August and 1% in September, in comparison to the previous month, expanded by 1.7% in October.

France

The French economy has registered steady growth with moderate inflation. Based on data free of seasonal factors, French GDP expanded by 1% in the third quarter in relation to the previous quarter. This result clearly reflected the effects of the growth in internal demand generated by higher wages and positive expansion in the export sector due, for the most part, to recovery in the countries of Europe and Asia. Private consumption expanded by 3.6% in the third quarter.

When measured by the consumer confidence index, expectations indicate that this trajectory will continue and will be fostered by the low level of French unemployment (11%) - considering historical figures - and by the already announced tax cut. Government estimates predict growth of 2.7% in 1999.

The consumer price index increased by 0.1% in October raising accumulated expansion to 0.7% in the year. Reflecting the increase in oil prices, the producer price index expanded by 0.6% in October.

Italy

The Italian economy was marked by clear signs of recovery in the activity level. Expressed in data purged of seasonal factors, industrial production grew by 1.4% in the third quarter, when compared to the previous quarter. The October consumer price index increased by 0.4% to 2.2% in twelve months. Producer prices reflected the rise in petroleum prices and expanded by 0.6% in October, raising accumulated growth in the last 4 months to 2.2%.

According to business confidence surveys, expectations indicate that the economy will expand at a more accelerated pace in coming months. However, the consumer confidence index dropped by 1.45% in November, as compared to an increase of 1.12% in October. This trajectory clearly reveals growth in political uncertainties and persistent concern with the ongoing reform of the social security system and the effectiveness of monetary policy.

3.4 - Emerging Asian economies

China

Growth of the Chinese gross domestic product closed the third quarter of the year at 7%, in comparison to the same period of the previous year. The second quarter had registered a rate of 7.6% indicating that the government will most likely attain its growth target of 7% for the year as a whole.

Industrial production increased by 7% in October when compared to the same month of the previous year, in contrast to 8.1% in September. This reduction can to some extent be ascribed to the prolonged holiday that marked the 50th anniversary of the communist revolution.

The process of economic recovery in the third quarter of the year was led by increases in internal and external sales. Following poor results in May, retail sales picked up in the month of July, reaching a growth level of 5.6%, with 6.3% in September, when compared to the same months of the previous year.

Public sector investments, which leveraged economic growth in the first half of the year, declined in the third quarter to a level 10.4% above the same period of 1998. Expansion in the first six months of the year had reached a level of 15.1%.

In the third quarter of the year, Chinese exports were 15.1% higher than in the same period of 1998, as compared to contraction of 2% in the second quarter of the year. The trade surplus closed at US$ 11.7 billion and surpassed that of the entire first half of the year (US$ 8 billion). Growth in foreign sales can be ascribed to recovery in the Asian economies, while expansion in internal sales was powered mostly by higher wages granted to civil servants and growth in the tax rate on time deposits, introduced as an instrument to stimulate families to greater consumption and less savings.

In October, the balance of trade came to US$ 4.4 billion, as compared to US$ 3.3 billion in September. This performance was based on exports of US$ 18.2 billion and imports of US$ 13.8 billion. It is estimated that recovery in the trade sector will generate a 1999 trade surplus of US$ 24.5 billion and could guaranty a current account surplus. This would obviously reduce the risk of the government implementing an exchange devaluation in the coming months.

Inflows of direct foreign investments in September were 13.9% higher than in the same month of the previous year. This level of capital movement has been stimulated by the permission granted to those holding direct foreign investments to deposit these funds in foreign currency, as collateral for debts contracted in the Chinese banking system. On effect of this measure has been to aid in sustaining the fixed rate of exchange.

Admission of China to the World Trade Organization (WTO) was made possible as a result of a trade agreement with the United States and is expected to generate increased imports and more voluminous foreign investments in the year 2000. For the most part, the increase in imports will result from elimination of quantitative quotas, while also reflecting cutbacks in tax rates and the expanded acquisitions of imported capital goods that are expected as a consequence of increased direct foreign investment.

Demand growth was not reflected in inflationary pressures. In October, the consumer price index declined by 0.6%, when compared to the same month of the previous year. This was attributed to growth in company productivity, particularly in the state companies that are going through restructuring processes. In September, the index decreased by 0.8%.

South Korea

Based on seasonally adjusted data, the South Korean GDP registered 3% growth in the third quarter, in relation to the previous quarter, and 12.3% in relation to the same quarter of the previous year. This performance reflects growth in the export sector. In the month of October, industrial production increased by 1.7% in the month and 30.6% in the year, as a result of 39% expansion in exports and 28% in domestic demand.

In October, the rate of unemployment fell to 4.6%, as compared to 4.8% in September. Between January and October, direct foreign investments totaled US$ 10.3 billion for a rise of 83% in relation to the same 1998 period. GDP is expected to increase by 9.5% in 1999, marking a significant reversal when seen against the 5.8% drop registered in 1998. This level of growth could certainly have an impact on the trajectory of inflation in 2000.

Malaysia

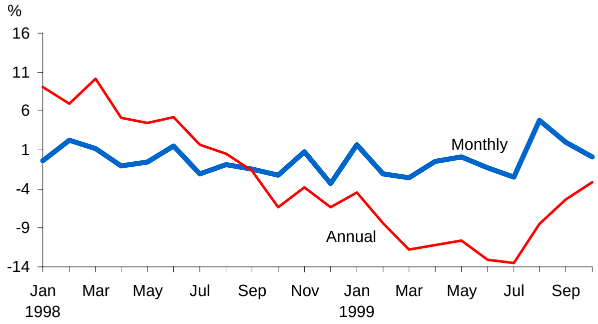
In comparison to a 7.5% figure in 1998, Malaysia is expected to register product growth of 4.3% in 1999. In the third quarter of the year, GDP expanded by 8.1% in relation to the same quarter of the preceding year. This was the highest rate of growth in the last three years.

3.5 - Latin America

Argentina

In the second quarter of the year, the Argentine GDP registered a decline of 4% when viewed against the backdrop of the same period of the previous year. The first quarter terminated with a 3% decline.

Industrial Production Index - Growth[1/]



Source: Ministry of Economy/Indec
1/ Seasonally adjusted.

However, considering seasonally adjusted data, monthly industrial production registered positive growth during three consecutive months, accumulating expansion of 6.9% between July and October. These figures clearly suggest that the cycle of declining expansion may finally have been reversed. In this sense, the production drop in relation to the same period of the previous year dropped from 10.8% in the first seven months of the year to 9.2% from January to October.

Investments dropped sharply, as evident in the 28.2% cutback in the production of the metal-mechanics industry, excluding automotive output, the 20% drop in imports of capital goods and the 35% reduction in imports of parts and accessories for capital goods. In data purged of seasonal factors, the construction activity index dropped by 0.7% in October, in relation to September, reflecting a 7.1% drop in accumulated terms from January to October, when compared to the same period of the previous year.

Supermarket sales accumulated in the first ten months of the year registered a reduction of 1.2% in relation to the same period of 1998, indicating a drop in consumption that was less than estimated for the GDP.

The trade balance turned in a deficit of US$ 292 million in the month of October, based on exports of US$ 1.9 billion and US$ 2.2 billion in imports. In the first ten months of the year, foreign sales totaled US$ 19.3 billion and imports came to US$ 20.9 billion, which were 15% and 22% less than in the same period of 1998, respectively. The major determinants of the drop in exports were reductions in international prices of primary products, with the exception of petroleum, and the Brazilian exchange devaluation, offset to some extent by the rechanneling of Argentine exports away from Mercosul, to the European Union.

The decline in imports was more accentuated under capital goods and their parts.

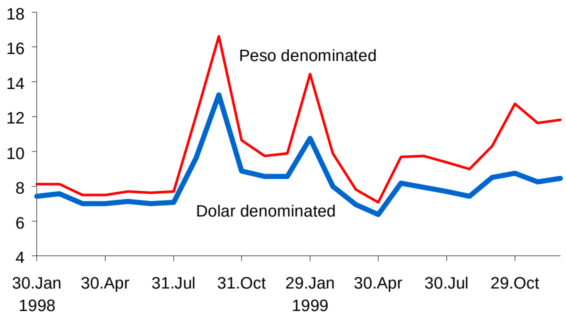
The consumer price index dropped by 0.3% in November, following stability in October. The wholesale price index fell by 0.2% in November, following a 0.1% reduction in October and a September rise of 0.9%, mirroring the impact of increases of 12.3% in the prices of primary fishery products and 12.2% under crude oil and natural gas prices in the month.

Based on the concept of average daily balances, financial system deposits increased by 0.1% in October, raising accumulated growth for the year to 5.8%, as a result of 13.5% expansion under foreign currency deposits and a 3.7% cutback in national currency deposits. Dollarization of fixed time deposits came to 76%.

International reserves of gold, exchange and central bank time deposits totaled US$ 23.2 billion, equivalent to total monetary authority financial liabilities, composed basically of the monetary base (US$ 14.2 billion) and net banking reserves (US$ 8.9 billion). With this, overall international financial system liquidity or, in other words, total central bank and financial institution foreign currency assets came to US$ 38.5 billion, equivalent to 41.1% of the broader monetary aggregate (M3*) which adds the monetary base to total demand and time deposits.

Interest Rate

(% per year)



Source: Ministry of Economy/B.C.R.A.

1/Buenos Aires Inter-Bank Offered Rate (Baibor), 30 days.

At a moment of governmental transition, uncertainties related to the fiscal situation together with interest rate increases in the developed economies were reflected in October growth in median interest rates in Argentina, principally in peso-denominated transactions. Consequently, the average monthly interbank interest rate (baibor) for 90 day operations in dollars increased from 8.78% per year in September to 9.38% per year in October, while the rate for peso operations moved from 11.81% per year to 13.42% per year. This movement resulted in an increase in the differential between the rates for the two currencies from 2.79% per year to 3.69% per year in the period. On October 29, this differential rose to 4.11% per year, similar to the level in effect in the critical moments of September 1998 and January 1999. However, though the average monthly rate has not yet been released, there are signs that this upward trend has been reversed, principally in the rates on transactions in United States dollars.

The central government financial result, which encompasses the National Treasury, decentralized organizations, social security system, public sector companies and provincial savings banks, closed with a negative US$ 838 million in October, raising the accumulated negative result in the first ten months of the year to US$ 2.3 billion.

The 1999 Argentine fiscal deficit will come close to US$ 5.8 billion, or approximately 13.7% above the target agreed upon with the IMF. Forecasts for the public deficit for next year indicate a level of US$ 10 billion, higher than the targets negotiated with the IMF and specified in the Fiscal Liability Act.

In this context, the new economic policy team has worked out an agreement with provincial governments regarding fund transfers. The agreement has already been approved by the Senate and is now under discussion at the Chamber of Deputies. Its terms state that the provinces will receive a monthly sum of US$ 1.35 billion in 2000 and US$ 1.36 billion in 2001. The central government will refinance provincial debts and absorb part of the deficits of regional social security systems. At the same time, the norms governing these systems will be altered to bring them more or less into line with the national system. The fiscal package includes an increase in internal taxes, generalized levying of the value added tax on private medical practice and transportation and increases in the income tax. The 2000 fiscal budget has not yet been approved by either house of Congress.

Mexico

In the third quarter of the year, Mexico turned in 4.6% GDP growth, in relation to the same quarter of the previous year, reflecting a process of recovery under services (4.8%) and manufacturing (5.3%). Retail sales expanded by 8.7% up to October, clearly demonstrating the impact of low interest rates and the downward trajectory of inflation on consumer spending.

The accumulated trade deficit up to October (US$ 2.5 billion) represents 40% of that registered in the same period of the previous year. In this sense, Mexican exports have benefited from the sustained growth of the American economy. Government estimates of 1999 GDP growth indicate a level of 3.4%, with inflation in the range of 12.9%.

Chile

Following the 1999 recession, there are signs of a turnaround in the economy of Chile. Based on data purged of seasonal factors, GDP expanded by 1.2% in the third quarter when compared to the previous quarter. This growth was favored by expanding copper exports. However, a comparison with the third quarter of 1998 indicates a 1.5% drop. In the month of October, industrial production expanded by 0.1% and unemployment dropped to 11%, in comparison to 11.4% in September. According to analysts, GDP growth for 2000 should close at approximately 5%.

Colombia

Colombia has experienced its worst recession in 70 years. GDP registered a 5% decline in the third quarter (preliminary data), as compared to negative rates of 5.9% and 7.6% in the first and third quarters of the year, when compared to the same periods of 1998. Expansion in the third quarter closed at 0.5%, compared to the second quarter.

3.6 - Conclusion

The outlook in the foreign sector is highly positive, with clear signs of an upswing in international economic expansion and consistent recovery in trade flows.

The United States economy continues barreling forward sustained growth by strong internal demand that does not yet seem to have responded to recent increases in interest rates decreed by the Federal Reserve. The optimistic expectations of the business community and consumers indicate that the high level of activity is not about to decline and this has been one of the mainstays of the growing recovery in world demand.

Japanese economic indicators show a turnaround, albeit at a less intense pace than in the final quarter of 1999. However, the upturn is still fragile since its momentum has depended on public sector outlays, while consumer spending and private investments have still not moved into a consistent growth trajectory. However, one should note that the confidence of businesspersons with respect to supply and demand conditions is relatively high at the same time in which the ongoing economic recovery in other Asian countries will certainly have a positive impact on Japanese exports and, therefore, on economic performance as a whole.

Indicators regarding the euro zone point to sustained growth rooted in strong internal and external demand, particularly in the German and French economies. With the positive outlook for continued economic expansion in the region, in a framework of an expanding monetary aggregate (M3) and acceleration in price growth in several different countries, the European Central Bank will have to keep a close eye on possible underlying inflationary pressures in the coming year.

The emerging Asian economies have definitely managed to turn their once floundering economies around, particularly in South Korea, China and Malaysia. Economic growth should continue in 2000 and will benefit principally from recovery in trade operations with the region's major partners.

In Latin America, the Argentine recovery is still surrounded by a good deal of uncertainty, particularly in terms of the rather serious fiscal difficulties faced by the authorities. At the same time, Chile has been impacted adversely by a downturn in its terms of trade. Growth in the region will undergo the negative effects of ongoing economic recessions in Colombia, Ecuador and Venezuela. However, to some extent this will be offset by positive growth in the Mexican economy, particularly as a result of the impacts of United States economic growth.

4 - Capital account

4.1 - Investments

Investments

US$ billion

Itemization	1998	1999					
		I Q	II Q	III Q	Oct	Nov	Jan-Nov
Foreign	24.3	7.9	6.4	9.8	2.1	2.5	28.6
Direct[1/]	26.1	7.7	5.4	9.6	2.1	2.3	27.1
Privatization	6.1	4.1	1.0	3.3	0.0	0.3	8.6
Conversions	2.2	0.8	0.9	1.3	0.3	0.6	3.8
Others	17.8	2.9	3.6	5.0	1.8	1.4	14.6
Portfolio	-1.9	0.2	1.0	0.2	0.0	0.2	1.5
Brazilian	-3.4	-0.7	0.6	-0.1	-0.8	-0.2	-1.2

1/ Includes reinvestments.

Up to the month of November, net direct foreign investment totaled US$ 27.1 billion in the year, 15.6% more than in the same period of last year. These resources have generated a gradual decline in the volume of external borrowing requirements which, in annual terms, moved from - 1.12% of GDP in November of last year to 0.84% of GDP in November of this year. Between August and November, monthly inflows remained above the level of US$ 2 billion.

Portfolio investments, which had registered net outflows in August, reversed course and racked up net inflows of US$ 326 billion in the month of September. The most important items here were net inflows to fixed income funds, which were partially offset by returns on investments in ADR, under the terms of Appendix V of Resolution no. 1,289/87. In October, stock investments (Appendices I to IV of Resolution no. 1,289/87) closed with negative net flows, while net inflows in ADR generated net inflows of US$ 8 million. In November, both of these asset headings closed with net investments: US$ 53 million in stocks and US$ 123 million in ADR.

4.2 - Loans and financing

Demand for funding sources to be used in paying medium and long-term liabilities, and current account obligations, remained on a downward trajectory. Amortizations paid in September and October were below average monthly amortizations for the first half of the year.

Uses and sources of foreign resources

US$ billion

Itemization	1998	1999 I Q	II Q	III Q	Oct	Nov	Jan-Nov
Uses	-67.2	-23.9	-16.8	-14.4	-5.1	-4.5	-64.9
Current transactions	-33.6	-5.2	-7.0	-4.6	-2.4	-2.2	-21.4
Amortizations	-33.6	-18.7	-9.9	-9.9	-2.7	-2.3	-43.5
Loans	-13.9	-12.8	-3.7	-4.0	-0.8	-0.8	-22.1
Public	...	-1.3	-1.2	-0.3	-0.1	0.0	-2.9
Private	...	-11.6	-2.4	-3.7	-0.7	-0.8	-19.1
Financing	-19.7	-5.9	-6.2	-5.8	-2.0	-1.5	-21.4
Public	...	-0.7	-1.0	-0.6	-0.4	-0.1	-2.7
Private	...	-5.2	-5.2	-5.3	-1.6	-1.4	-18.7
Sources	67.2	23.9	16.8	14.4	5.1	4.5	64.9
Direct investments[1/]	26.1	7.7	5.4	9.6	2.1	2.3	27.1
Investments in portfolio	-1.9	0.2	1.0	0.2	0.0	0.2	1.5
Import financing	23.5	4.7	4.0	4.2	1.2	2.3	16.3
Long-term loans	41.7	2.7	9.4	3.9	1.2	2.7	19.9
Short-term capital (net)	-27.3	-0.6	-2.1	-1.6	-0.2	-0.4	-4.8
Sundry[2/]	-12.2	-1.2	-1.7	-0.6	-0.4	-0.3	-4.2
Change in reserve (-=increase)	17.3	10.5	0.9	-1.2	1.2	-2.3	9.0
Net Reserves	34.4	24.1	23.3	24.5	23.3	26.0	26.0
RLA (Memorandum)	34.4	24.1	23.3	24.8	22.2	20.6	20.6
Regularization Operations	9.3	0.0	8.5	0.0	-1.5	0.0	7.0
International Liquidity	44.6	33.8	41.3	42.6	40.1	42.2	42.2

1/ Includes reinvestments.
2/ Includes Brazilian investments abroad, constitution of collateral, Brazilian financing to foreigners, other capitals, errors and omissions and Banco Central's liabilities.

Disbursements of financing closed with a stable performance. Loans turned in growth in both September and October. The causes of the aforementioned expansion were greater placements of notes and commercial papers and issue of bonds of the Republic, with an inflow of US$ 532 million in September. In the month of October, a new US$ 2 billion issue of bonds of the Republic was made in exchange for securities involved in the renegotiation of the nation's foreign debt, with a face value of US$ 3 billion.

This growth trajectory continued in November, as loan and financing disbursements expanded. Inflows of financing closed at US$ 2.3 billion, of which US$ 1.1 billion involved IDB credits. Medium and long-term loans totaled US$ 2.7 billion, for growth of US$ 1.5 billion in relation to the month of October. For the most part, this was due to placements of US$ 1.3 billion in bonds of the Republic. Inflows through notes registered growth of US$ 72 million, while those resulting from operations with commercial papers and bank loans increased by US$ 25 million and US$ 193 million, respectively. Intercompany loans declined by US 113 million.

Amortizations of loans dropped sharply as a result of lesser payments of notes in the month of October, a period in which there was an increase in amortizations paid to commercial banks. This increase was concentrated in payments of loans for onlending operations to companies in the country (Resolution no. 63) and of commercial bank loan principal in the month of November.

Amortizations of medium and long-term financing registered declines in both October and November and a similar performance is expected in the month of December. The reason behind this performance is that, in the month of December of last year, suppliers' and buyers' credits dropped sharply and payment of these operations normally have 12 month payment schedules.

4.3 - Conclusion

Cutbacks in demand for exchange coupled with access to permanent sources of financing have diminished pressures on exchange in recent months and have even generated some degree of valuation. Direct foreign investments that are not part of the privatization process have remained high and, in annual terms, have surpassed the volume of the current account deficit.

New inflows through bonds of the Republic, which have been insufficient to meet demand, have demonstrated that these operations are an important source of financing. Parallel to this, the increase in the volume and average terms of funding contracted by the private sector shows that, in comparison to recent months, financing of the balance of payments will certainly be a much easier process. Aside from this fact, the volume of foreign liabilities with average redemptions terms between one and two years and paid off in the current year means that there will be lesser demand for funding in the coming months.

5 - Prices

Inflation in the first quarter of the year moved sharply upward as a consequence of the exchange devaluation. However, in the subsequent quarter, the rate settled back as the effect of devaluation was absorbed by the economy. At the end of the first half of the year and start of the second half, inflation peaked once again as a result of fuel price hikes, public tariff adjustments and higher prices for farm products and medicines.

The upward price movement registered in the third quarter of the year continued in October and November, mostly as a consequence of increases in farm prices. This performance mirrored the falloff in supply caused by the impact of unfavorable seasonal factors on the harvest, by strong growth in export operations and by low buffer stock levels of these goods.

5.1 - General indices

In both October and November, general price indices calculated by the Getúlio Vargas Foundation followed a rising curve as price increases accelerated at both the wholesale and retail levels. Growth in wholesale prices is explained by the prices of farm products, which accounted for the sharpest increases in the period, and industrial goods, which were pressured by higher prices for raw materials and the exchange devaluation. In twelve month terms up to November, growth of the IGP-10 came to 17.2% while the IGP-M rose by 18.5% and. the IGP-DI accumulated expansion of 19.7%.

General indices

% growth

Itemization	1999				
	Jul	Aug	Sep	Oct	Nov
Monthly					
IGP-10	1.4	1.6	1.5	1.5	2.2
IPA	1.8	2.1	2.2	2.3	3.0
IPC	1.0	1.0	0.4	0.3	1.0
INCC	0.3	0.5	0.8	0.9	1.1
IGP-M	1.6	1.6	1.5	1.7	2.4
IPA	2.0	2.2	2.2	2.5	3.3
IPC	1.1	0.7	0.4	0.6	1.2
INCC	0.4	0.5	0.8	0.8	1.2
IGP-DI	1.6	1.5	1.5	1.9	2.5
IPA	2.0	2.2	2.3	2.6	3.6
IPC	1.2	0.5	0.2	0.9	1.1
INCC	0.5	0.7	0.9	1.0	0.9

Source: FGV

Changes in the IPC-Fipe weighting structure

The consumer price index of the Municipality of São Paulo was first calculated in January 1939 and is the country's oldest inflation index. It was calculated by the local government administration until 1968 when this task was transferred to the Institute of Economic Research of the University of São Paulo, later transformed into the Institute of Economic Research Foundation (Fipe). This index calculates price variations for a grouping of basic consumer products in a framework of families with income levels from 1 to 20 times the minimum monthly wage.

Since January 1994, the IPC-Fipe has been calculated through use of the weighting system used in the Family Budget Survey taken between March 1990 and February 1991. As of January 2000, the IPC-Fipe weighting structure will be altered to reflect the results of the Family Budget Survey (POF) dated 98/99. Evidently, the new survey was designed to incorporate changes in consumer habits among families living in the municipality.

Periodic updating of the weighting structure is a normal procedure, since consumer habits tend to change over time. Among the new items to be incorporated into the Fipe price gathering process will be outlays on cell telephone service, computers, cable TV and the Internet.

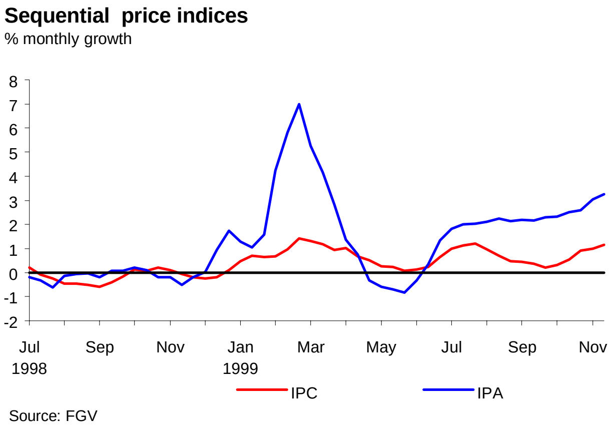
The following table presents the weights of the major IPC-Fipe components based on the 90/91 survey and used to calculate the index in the period from January 1994 to December 1999, together with those to be applied in the 98/99 survey.

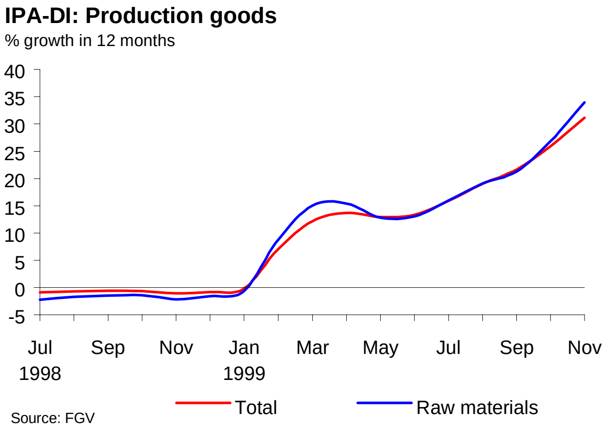
Weighting Structure - IPC-Fipe

Grouping	POF (91/92)	POF (98/99)
Housing	26.5	32.7
Food	30.8	22.7
Transportation	12.9	16.1
Personal expenditures	12.5	12.3
Health	4.6	7.0
Apparel	8.6	5.3
Education	3.9	3.8

Source: Fipe

Among the elements included in the new structure, one should highlight sharp growth in the participation of spending on housing and lesser participation under food and apparel. This change is expected to make the index less susceptible to seasonal factors, particularly during the agricultural off-season and periods of changing fashions. At the same time, in the grouping transportation, lesser weight is ascribed to "fuels", since this is an item strongly impacted by exogenous factors. This change should also aid in smoothing out the ups and downs of the index. Finally, one should note that the new weighting structure of the IPC-Fipe will bring that index closer to the structure used in the IPCA, which was altered in August of this year by IBGE.





In the concept of domestic supply, the IPA was more strongly impacted by the prices of production goods, particularly raw materials, followed by construction industry inputs and machines, vehicles and equipment. In the heading of consumer goods, the performance of the farm sector forced a rise in food prices, while termination of the automotive agreement and cancellation of levying of reduced IPI rates, accompanied by the consequent elimination of ICMS incentives in the State of São Paulo required restructuring of tax rates on the automotive industry and, therefore, brought added pressure to bear on price indices. On a product-by-product basis, the largest price increases occurred under coffee beans, cattle, swine, poultry, corn, sugarcane, sugar, pulp, paper and cardboard, alcohol, automobiles, industrial machines and equipment and plastics.

5.2 - Consumer price indices

Consumer prices — % growth

Itemization	1999 Jul	Aug	Sep	Oct	Nov
Monthly					
IPCA	1.1	0.6	0.3	1.2	1.0
IPC-Fipe	1.1	0.7	0.9	1.1	1.5
IPC-Br	1.2	0.5	0.2	0.9	1.1
Accumulated in the year (annualized)					
IPCA	8.9	8.6	8.1	8.8	8.3
IPC-Fipe	6.3	6.7	7.2	7.9	8.1
IPC-Br	9.7	9.3	8.5	8.8	8.5
12 months					
IPCA	4.6	5.7	6.3	7.5	8.6
IPC-Fipe	1.4	3.1	4.8	5.9	8.0
IPC-Br	4.9	6.0	6.4	7.2	8.6

Source: IBGE, Fipe and FGV

At the end of the third quarter of the year, consumer price indices decelerated, as the impact of increases under fuel prices and public tariffs were fully absorbed by the economy. In October and November, higher prices for beef, chicken, sugar, alcohol, gasoline and automobiles accounted for the major share of inflation. Accumulated 12 month rates up to November came to 8% for the IPC-Fipe and 8.6% for the IPC-Br and the IPCA.

The fact that wholesale and consumer price indices have been following generally distinct trajectories in the recent past has been interpreted by some observers as an element that could well potentialize inflation rates to be perceived in the near future by consumer price indices.

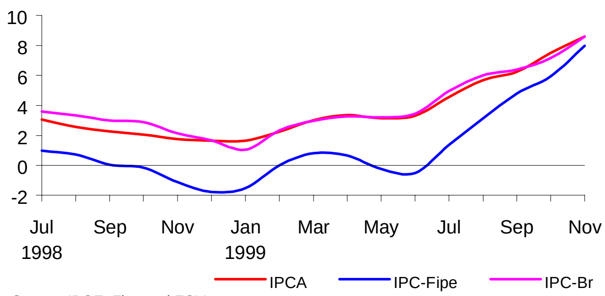
Major items affecting November price indices

%

Itemization	IPCA			IPA-DI			IPC-BR			IPC-Fipe		
	% Change	Weight	Contri-bution	% Change	Weight	Contri-bution	% Change	Weight	Contri-bution	% Change	Weight	Contri-bution
Index (A)	**0.95**	**100.00**	**0.95**	**3.59**	**100.00**	**3.59**	**1.12**	**100.00**	**1.12**	**1.48**	**100.00**	**1.48**
Items												
Cattle	5.00	2.84	0.14	4.23	7.16	0.30	4.44	2.47	0.11	4.55	4.50	0.20
Poultry	8.00	0.93	0.07	10.79	1.30	0.14	5.98	1.01	0.06	10.95	1.64	0.17
Eggs	4.19	0.20	0.01	10.66	0.91	0.10	...	...	...	...	...	...
Swine	...	...	...	11.18	1.21	0.13	7.65	0.23	0.02	...	...	...
Corn	...	...	...	17.74	1.91	0.34	...	...	...	...	...	...
Coffee (in beans)	...	...	...	32.50	1.20	0.39	...	...	...	...	...	...
Sugarcane	...	...	...	5.46	2.55	0.14	...	...	...	...	...	...
Cassava	...	...	...	39.73	0.84	0.33	...	...	...	...	...	...
Oranges	...	...	...	33.76	0.85	0.29	...	...	...	...	...	...
Papaya	...	...	...	18.33	0.89	0.16	9.11	0.31	0.03	...	...	...
Sugar	6.15	0.38	0.02	...	...	...	8.53	0.32	0.03	6.66	0.75	0.05
Alcohol	30.33	0.69	0.21	15.01	0.97	0.15	36.93	0.69	0.25	33.59	1.46	0.42
Gasoline	4.60	3.44	0.16	...	...	...	4.37	3.07	0.13	5.18	3.07	0.16
Fuel oils	...	...	...	6.97	1.32	0.09	...	...	...	...	...	...
Fuel for leisure transportation	...	...	...	...	...	...	...	...	...	12.21	0.41	0.05
New automobile	...	...	...	...	...	...	3.14	1.27	0.04	...	...	...
Apparel	0.61	5.64	0.03	...	...	...	1.14	5.46	0.06	...	...	...
Total (B)	**...**	**14.12**	**0.65**	**...**	**21.11**	**2.56**	**...**	**14.82**	**0.73**	**...**	**11.83**	**1.04**
Participation (B/A)	**...**	**...**	**0.68**	**...**	**...**	**0.71**	**...**	**...**	**0.66**	**...**	**...**	**0.71**

Source: IBGE, FGV and Fipe

Consumer prices
12 month % change



Source: IBGE, Fipe and FGV

However, closer attention should be paid to the fact that exportable goods play a much larger role in wholesale price indices and, by their very definition, are significantly more susceptible to exogenous price shocks and exchange devaluations. On the other hand, the participation of these items in consumer price indices is much more restricted, as exemplified in the fact that they account for just 44% of the composition of the IPCA. In the case of this index, the most important items are nontradable goods and services (31.8%), such as in natura foodstuffs and services, and government managed prices (24.2%), such as public tariffs and the prices of public services, both of which are subject to government intervention.

Analysis of price growth at the start of the period of the real sheds light on the current discussion of the possible existence of repressed inflation, in the case of consumer prices. In this light, one should recall that the greatest inflationary pressures in the early months of the real were generated precisely by nontradable goods and services. These prices accumulated strong gains in relation to tradables which, in turn, were forced downward as the value of the nation's currency gained in value. With adoption of a floating rate of exchange in early 1999, changes in the prices of these products have been below average and have acted as a cushion capable of absorbing the effects of the process of relative price alterations caused by devaluation of the real.

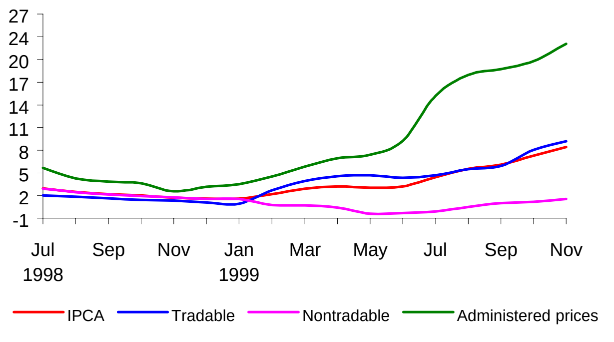
In this framework, in which changes in the prices of nontradables have lagged behind those of tradables, the two indices will begin to converge when the more accelerated pace of wholesale price growth begins slowing, provided that the process is not impacted by such unexpected exogenous factors as, for example, further oil price hikes.

At the same time, one should consider the higher degree of aggregation that marks final consumption products that form the basis of consumer price surveys, in contrast to the type of product included in wholesale price indices. The cost composition of consumer indices is composed mostly of goods and/or services that are not overly impacted by exchange rate variations, external or seasonal factors. Therefore, these goods are not susceptible to price pressures with the same magnitude of the products covered by wholesale price surveys.

Broad National Consumer Price Index (IPCA)

For the most part, acceleration of the IPCA in October was due to increases in the prices of foodstuffs and new automobiles, which generated the highest single impact on the index. This impact also contributed to sharper price growth under tradable goods, mostly because the survey stipulates that the prices stated on company price tables are to be used in these calculations, without taking account of discounts so frequently granted to consumers. Aside from this, another important contributing factor were industrialized foods prices, such as sugar and bakery goods, and the prices of semiprocessed goods, such as grains and meats. In

Consumer prices
12 month % change



IPCA % growth

Itemization	1999				
	Jul	Aug	Sep	Oct	Nov
Month					
IPCA	1.1	0.6	0.3	1.2	1.0
Tradable	0.3	0.3	0.3	2.2	1.0
Nontradable	-0.1	0.2	0.1	0.2	0.2
Administered	5.9	1.6	0.6	0.8	1.9

Source: IBGE

the opposite sense, falloffs under in natura food prices, rents and personal services made it possible to hold changes in the overall prices of nontradable goods to reasonably low levels. In the month of Nevember, IPCA was particulary affected by increases in gasoline and fuel alcohol prices, which accounted for 0.37 percentage point of that index.

IPC-Fipe

In October and November, São Paulo inflation, measured by the IPC-Fipe, basically reflected the trajectory of outlays on food and transportation, areas in which the largest increases were limited to a small number of products. One should emphasize that beef, chicken, sugar, alcohol and gasoline, taken by themselves, accounted for more than 70% of the growth in the index.

5.3 - Government managed prices

The weights of government managed prices - prices of goods and services directly or indirectly determined by federal, state or municipal governments - account for approximately 20% of consumer price indices.

It is interesting to note that, in the course of 1999, various factors accounted for the high level of participation of these prices in inflation, as measured by consumer indices. Thus, in the case of IBGE indices, this participation came to approximately 40% and as high as almost 50% in the IPC-Fipe.

The trajectory of these prices in 1999 must be analyzed in light of economic circumstances that have a direct or indirect impact on their evolution. One should note that the strong increase in fuel prices was generated by highs in international oil prices and the exchange devaluation that occurred in the year. Both of these factors would tend to be neutral or even to have a positive impact in the coming year. In 1999, these factors had a strong impact on the prices of petroleum derivatives which accumulated increases of 51.3% (diesel oil) and 182.3% (LPG) at prices in the oil refinery.

For consumers, the rise in international petroleum prices resulted in upward movement in gasoline and cooking gas prices of approximately 50% and 40%, respectively. Aside from this, urban transportation costs - a very important item in consumer price indices - were also pressured by the rise in diesel prices.

Administered prices: major items affecting inflation indices in 1999 [1/]

Items	IPCA			INPC			IPC-Fipe		
	Weight [2/]	Accumulated	Accumulated sharing	Weight [2/]	Accumulated	Accumulated sharing	Weight [2/]	Accumulated	Accumulated sharing
Index (A)	100.00	8.29	8.29	100.00	7.63	7.63	100.00	8.11	8.11
Urban transportation [3/]	4.28	14.25	0.55	7.84	13.74	0.91	4.80	15.09	0.68
Gasoline	3.44	50.79	1.47	1.84	50.91	0.68	3.07	52.54	1.30
Alcohol	0.69	32.11	0.20	0.12	47.55	0.05	1.46	49.27	0.59
Barreled cooking gas	1.11	43.67	0.32	1.87	42.20	0.53	0.68	36.70	0.21
Electric energy	3.31	19.19	0.35	4.40	17.28	0.38	3.85	20.95	0.74
Telephone	2.86	8.83	0.17	1.30	10.68	0.08	0.92	0.12	0.00
Water supply and sewerage taxes	1.54	10.53	0.13	2.10	9.97	0.17	2.83	16.92	0.44
Total (B)	**17.22**	**...**	**3.19**	**19.47**	**...**	**2.79**	**17.60**	**...**	**3.96**
Sharing (B/A)			**0.38**			**0.37**			**0.49**

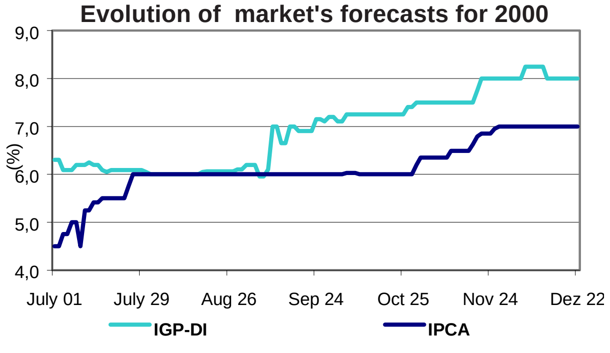
1/ Up to November.

2/ November weights.

3/ INPC and IPCA refer only to urban bus services.

Electric energy tariffs, which account for an important share of consumer price indices, increased at rates higher than the consumer price indices themselves, as a result of the impact of the exchange devaluation on supply costs and of growth in the General Price Index - Market (IGP-M), the parameter utilized for adjusting the sector's tariffs. One should stress that, for 2000, exchange rates and the results of general price indices will tend to generate lesser increases in these tariffs.

5.4 - Market expectations



Market expectations on inflationary tendencies for the next year is a relevant topic to understand the country's economic fundamentals. In a context of enhanced market integration, the Banco Central carries out a daily survey - with an average sample including seventy financial institutions and consulting agencies - aiming at forecasting inflation rate expectations for the year 2000.

Market inflation expectations are defined as the mean point of projections released by financial institutions and consulting agencies. Thus, for the year 2000, expected inflation , when measured by the IPCA index, reached 7% at the beginning of December, after becoming stabilized at 6% from August until mid-October.

With regard to the general indices - particulay hose expectations concerning the IGP-DI performance - they may evolve in a similar fashion as the IPCA, despite their level has moved up from 6% p.y. to 8% p.y. since the last two months.

Even though index forecasts rose slightly during the month of November, they remained considerably lower than those observed during the current year, thus underlining market confidence in a favorable developments of the Brazilian economy during the year 2000.

5.5 - Conclusion

Just as in the third quarter of the year, sources of major inflationary pressures in October and November were mostly sector-specific and transitory, particularly in the case of farm prices. As the harvest off-season period draws to a close, the outlook for the month of December is more favorable, despite pressures caused by seasonal consumption. Following that period, the situation in the early months of next year should be much more favorable as the summer harvest is gathered and the supply flow of farm products is normalized.

Consequently, one can expect a substantial decline in inflation rates as of the month of December and this is already evident in market estimates for price indices. Taking due account of forecasts for December, accumulated rates for 1999 will close in the range of 20% for general price indices and 9% for consumer price indices. For the first quarter of next year, estimates suggest a downward trend in consumer price indices.

6 - Prospects for inflation

This chapter of the *Inflation Report* presents the Monetary Policy Committee's (Copom) assessment of Brazilian economic performance since the September *Inflation Report*, together with its prospects for inflation up to 2001. The projections are based on the assumption that the basic interest rate will remain unchanged during the period under analysis at 19% per year, rate set by Copom in its December 15th meeting. It is important to note that this is a strictly technical procedure. Hence, this hypothesis should not be taken as a forecast of future interest rate outcomes.

The inflation and output growth forecasts presented in this *Report* are not meant to be restricted to point estimates. They are projected within confidence intervals, reflecting the degree of uncertainty when setting the basic interest rate. Inflation forecasts are based not only on a fixed nominal interest rate, but also on the baseline scenario, summarizing the future behavior of key economic variables and their associated risks. The forecasts are presented in this *Report* in order to enhance monetary policy transparency, easing its task to maintain inflation under control.

Brazil is the first country whose inflation targets are included as indicative targets in an agreement with the International Monetary Fund (IMF). The adoption of this criteria is appropriated in the context of the new inflation targeting framework.

The quarterly targets agreed upon in the fourth review of the Economic Program with the IMF are fully consistent with the annual target defined for 2000 by the National Monetary Council, on the terms of Decree No. 3,088, of June 21, 1999. The quarterly targets refer to the 12-month IPCA inflation. The targets for each quarter of 2000 are 7.5%, 7.0%, 6.5% and 6.0%, respectively. Besides, two bands were defined around these targets. The inner encompasses +/ - 1 percentage point, while the outer covers a +/- 2 percentage points.

6.1 – Determinants of inflation

Aggregate demand and aggregate supply

Important changes have occurred in the economic environment since the September *Report*. Aggregate demand has continued its slow recovery and, over the medium-term, is not perceived as a source of pressure on prices. However, in the last quarter of the year, the economy was hit by negative supply shocks not foreseen in the last issue of the *Report*. Therefore, the baseline scenario for the coming quarters has changed significantly.

The first shock was the crop and livestock off-season, much harsher than usual. The second was the hike in fuel alcohol prices due to increase in international sugar prices. The increase in fuel alcohol also impacted gasoline prices. The third shock was expiration of the automotive agreement between the government and vehicle manufacturers, which eliminated the industrialized products tax–IPI reduction on new cars. The tax increase was passed through to consumers and auto prices rose in October. In spite of the impact on inflation, this episode highlighted an idiosyncrasy of the IBGE methodology. IBGE collects suggested prices by the manufacturers without taking discounts into consideration. Therefore, the actual rise in new car prices was far smaller than that measured by IPCA. Moreover, the increase in prices was fully captured in a single month.

The outcome of these shocks has been the jump in consumer price indices since October not anticipated in the last *Inflation Report*. In October, IPCA registered the highest rise for the year, 1.19%. Due to the nature of these shocks, their impact on inflation should be temporary. In other words, there is no mounting inflationary process underway. This diagnosis is already confirmed in November, when inflation (0.95%) dropped in relation to the previous month. For December inflation must be even lower.

The feature that has drawn the greatest attention is the behavior of government managed prices. Copom has recently quantified the impact of these prices on inflation. They encompass public utility services that were recently privatized, including power and telephone services. The adjustments in these prices have been much larger than inflation measured by consumer price indices, as they follow contractual clauses and not market conditions (see box on Government Managed Prices).

The impact of this shock on inflation in 1999 has been far from negligible. Out of the 8.29% IPCA inflation between January and November, 3.5 percentage points are directly due to government managed prices.

At the beginning of 2000, a more pronounced drop in inflation is expected as a result of several positive events. Farm product prices will fall as the new harvest reaches the market. Also, meat prices will decline due to the end of the off-season period. Actually, meat price has already declined in December and further reductions are expected for the coming months.

The recent evolution of the exchange rate is another element expected to help driving farm prices downward. In the coming year, lower foreign debt amortization together with an expected trade balance recovery should positively impact the FX market. The surge in commodity prices, however, can offset in part the trend of downward farm prices.

On the other hand, oil price, which reached its highest level since the Gulf War, is expected to drop during the year. The baseline scenario put forward in the last *Report*, which states that oil prices will remain high in the first quarter of 2000, during the winter period in the northern hemisphere, is maintained. Prices are expected to turn downward after April in such a way to become no more than a moderate source of concern in 2000.

The drop in unemployment rate at the end of this year was caused by seasonal factors. Seasonally adjusted figures show that jobless rates remain high. The stronger economic recovery expected for next year will help increasing employment levels.

Aggregate demand has been recovering gradually and does not represent any major concern in terms of inflation. Even with the recovery expected in 2000 (see GDP Growth Fan Chart), an imbalance between aggregate supply and demand is not likely, once the high level of idle capacity in the economy is considered.

As noted in the last issue of the *Report*, the economy in 2000 will benefit from export growth and increased credit supply. The segments of consumer durables, capital goods and housing, which were singled out in the September *Report* as having the greatest growth potential in the coming year, have already shown expansion. In October, industrial production grew 1.6%. Based on seasonally adjusted data, consumer durables increased by 4.2%, with particularly strong growth under electric-electronic goods (8.2%). Capital goods and construction grew by 3.1% and 2.9%, respectively.

Trade balance forecasts in the wake of January devaluation were thwarted and 1999 will end posting a deficit, albeit significantly smaller than in 1998. Despite of that, there is little doubt that next year's trade balance will be positive, due to three factors. First, the experience of several countries, as well as Brazilian past devaluation experience, shows that the impact of exchange rate devaluations is spread out over time. Second, commodity prices that had been declining steadily after the Asian crisis have turned upward. Finally, higher international economic growth, particularly in Latin America, should foster demand for Brazilian manufactured goods, which have been seriously hit by the adverse 1999 external outlook

Fiscal policy will continue as one of the cornerstones of price stability. In 1999, Brazil fully complied with its fiscal targets and the same is expected for next year. The strong primary surplus in 1999 was reached in an environment of weak economic activity and notwithstanding reductions in revenues as those of public service concessions in telecommunications. In 1999, these revenues totaled R$ 5.2 billion or R$ 6.5 billion less than in 1998. Furthermore, the fiscal performance has improved the "Brazil risk" premium.

However, one should note that next year's local elections require special concern regarding public sector spending. It is essential to keep the current commitment to austerity as a fundamental component of macroeconomic policy.

International economy

The external scenario is by no means free of risks, although attenuated in comparison to those foreseen in the September *Report.* The major source of uncertainty is still the possibility of a sudden deceleration of the United States economy. This could be triggered by a higher-than-expected interest rate hike or a stock market plunge with undesirable impacts on consumption. Though growth is still robust and unemployment rate has fallen to a record low, the quality of the expansion, based on sound fiscal accounts, increased investments and high productivity gains, suggests a gradual deceleration for next year. As foreseen in the September *Report*, the Federal Reserve increased the federal funds target rate by 25 basis-points to 5.50%, the level prior to the Russian crisis. An additional increase of 75 basis-points, already priced in the futures market, is expected for 2000.

As stated in the September *Report*, recovery in the Japanese economy is still fragile. This diagnosis was confirmed by the announcement of a 1% drop in third quarter GDP following strong first half-year growth. Though this result does not change the growth forecast for 2000, caution is advisable. Private demand is vigorous and the new set of fiscal measures announced in November should foster economic activity in the coming year.

In Asia, the countries hit by the 1997 crisis have achieved a remarkable turnaround, particularly South Korea and Thailand. The expected growth for the region will certainly enhance international trade and, particularly, the Japanese foreign trade. As Asia is an important market for Brazilian goods, recovery will certainly have a positive effect on Brazil's trade balance.

In much the same way, the growth outlook for the Euroland next year has improved. Though devaluation of the euro against the dollar was unexpected, it has contributed to the economic expansion. With growth in output, the European Central Bank raised interest rates by 50 basis-points at its second-to-last meeting. One cannot ignore the possibility of new increases in the coming year, particularly if devaluation of the euro continues, a process that could lead to higher inflation. The European Commission predicts 3% growth in 2000 compared to 2.1% for 1999.

Considering unemployment rate at the lowest level since the 1970's and a sharp growth in domestic demand (4.5% for the second quarter), the Bank of England decided in its November meeting to act preemptively and raised the basic interest rate to 5.5%.

Regarding other emerging economies, the outlook for 2000 points to improvement in economic performance, as recently demonstrated by the strengthening of sovereign bonds. Uncertainties associated to Argentina have substantially decreased following the election of the new president.

In a nutshell, one can expect stronger growth in the world economy and in Latin America in 2000 with positive impacts on commodity prices and demand for Brazilian manufactured goods. The external risks in the baseline scenario are considerably lessened compared to the last *Inflation Report*.

6.2 – Baseline scenario: assumptions and associated risks

Despite October and November consumer price hikes, the economy is not under a mounting inflationary process. Inflation should drop in December and fall even more in the early months of 2000, when the new harvest reaches the market.

Domestically, the major source of concern is that of government managed prices as they are adjusted according to contract clauses and not market conditions (see Box on Government Managed Prices). The prices of those services that are in part indexed to general price indices, may rise at a higher rate than average consumer prices (reflecting the 1999 behavior of the general price indices). However, the impact of these prices on the IPCA will not be as strong as it was in 1999. The baseline scenario also assumes moderate growth in prices fixed by local governments, such as real estate and land taxes and urban transportation fares, as a consequence of the upcoming municipal elections scheduled for the second half of the year. Under a conservative approach, the underlying assumption for all government managed price adjustments averages 9.2%, with a direct impact of 2.3 percentage points on IPCA next year.

Growth for the coming year is not expected to fuel inflation since, after two years of low GDP growth, there is still considerable idle capacity in the economy.

Simultaneously, undue pressures are not expected under food prices. In the first quarter of 2000, declines can be expected under several important products, particularly meat. However, for the year as a whole, farm prices are expected to have a neutral impact on inflation. On the one hand, the 2000 harvest will be quite similar to 1999. On the other hand, commodity prices will move moderately upward, following more intense international economic growth. Though this would normally tend to pull inflation up, current price indices have already incorporated increases of such major products as coffee and soybeans. Moreover, increased commodity prices will favor the trade balance, impacting positively the FX market. These factors should be mutually offsetting and farm supply is not identified as a source of inflationary pressure.

The external environment looks favorable for the FX market. Trade balance is expected to improve and inflows of capital to Brazil should continue at their current level or even improve. As for the trade balance, the greatest risk is that of a new oil price hike. The price might reach as much as US$ 27 per barrel in the first quarter of the year before settling back into the range of US$ 20 to US$ 22 as the winter in the northern hemisphere ends.

If, on the one hand, growth in world oil prices will exacerbate pressure on Brazilian imports, the export sector will benefit from the added international economic growth forecast for 2000. At the same time, stronger international growth should increase volume and world prices of the major commodities exported by Brazil.

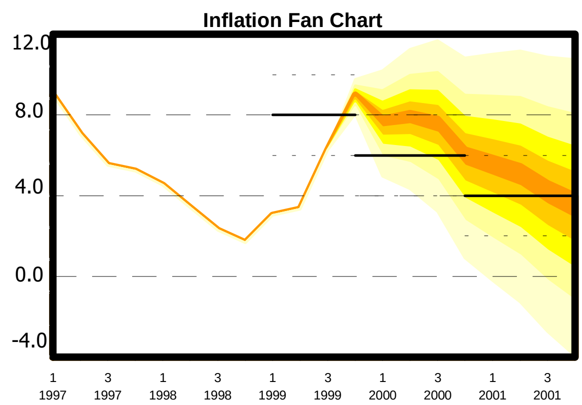
Foreign capital inflows, a relevant factor for the exchange rate path, depends heavily on the "Brazil risk" premium. The major determinants of the country risk are international liquidity conditions, fiscal policy results and the expected current account balance. A reduction in the current account deficit is foreseen as a consequence of the trade balance improvement. Insofar as fiscal policy is concerned, the baseline scenario assumes continuos primary surpluses, fully meeting the targets set out in the Economic Program.

Regarding international liquidity conditions, the main risk refers to the US basic interest rates. Based on future markets, federal funds rate shall rise gradually from the current level of 5.50% per year to 6.25% per year in the third quarter of 2000, in quarterly 25 basis-point increases.

Several factors should concour to increase international liquidity: the removal of the Y2K hurdles, world economic growth and improved emerging markets risk perception, more than offsetting negative effects of US interest rate hikes. Accordingly, a slight drop in the "Brazil risk" can be expected over the course of the year.

6.3 - Inflation forecast

Forecasted IPCA-Inflation with interest rate fixed at 19% p.y.



(accumulated inflation in 12 months)

Based on available information and the assumptions with associated risks considered by Copom, a projection of the 12-month IPCA inflation rate was constructed, considering the constant 19% per year interest rate set out at the Committee's December 15th meeting.

This projection incorporates the impact of government managed prices as follows. The first step is to project inflation according to the baseline scenario but with no hypothesis regarding government managed prices. This is akin to state that these prices will behave like the average of other prices in the economy. The following step is to add to each quarter the difference between the projected inflation rate and the overall out-of-the-model adjustment in government managed prices. This difference is then

IPCA with 19% fixed interest rate

Year	Q	Confidence Intervals						Central Projection
		50%						
			30%					
				10%				
1999	4	8.6	8.7	8.8	9.0	9.1	9.3	8.9
2000	1	6.5	7.0	7.4	7.8	8.2	8.6	7.6
2000	2	6.4	7.0	7.5	8.1	8.6	9.2	7.8
2000	3	5.7	6.5	7.1	7.8	8.4	9.2	7.4
2000	4	3.8	4.7	5.5	6.2	7.0	7.9	5.8
2001	1	3.1	4.1	5.0	5.8	6.7	7.7	5.4
2001	2	2.4	3.5	4.5	5.4	6.4	7.5	4.9

Note: Accumulated inflation in 12 month, in % p.y. The values correspond to the ones shown in the inflation fan chart

duly weighted and incorporated into the model. The result is an expected set of quarterly shocks, with a probability distribution as assessed by Copom.

As in previous *Reports*, the trend for inflation is downward for the most of the forecasting period, with a substantial drop in the first and fourth quarters of 2000. It should be noted that, for both 2000 and 2001, the 30% confidence interval around the median is almost completely within the tolerance band for the respective annual targets.

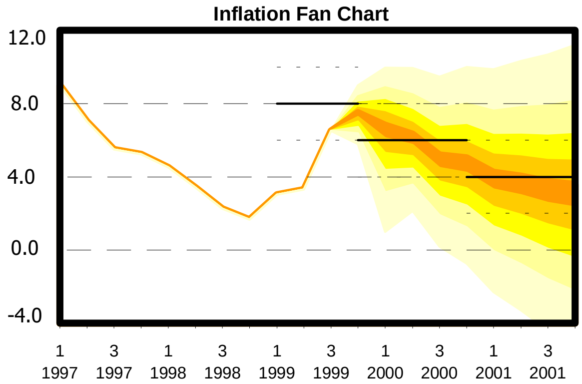
However, one should warn that this path for inflation reflects significant risks in terms of compliance with the quarterly indicative targets for June and September 2000. This is due to a statistical effect and to the magnitude of the government managed price shocks. Twelve month inflation rate should fall in the first quarter of the year as the lower price increases for early 2000 gradually substitute the highs registered in the same period of previous year. In the second quarter, even if inflation keeps its positive 1999 performance (1.06% from April to June as a consequence of the favorable farm goods price shock), 12-month variation will stabilize instead of following the declining targets. In the third quarter, utility price increases will rise inflation, albeit at a lesser pace than in 1999. The result will be a drop in the 12-month rate, though this decline may not be enough to avoid hitting the upper limit of the inner band. However, the projection for the end of 2000 is slightly below the 6% target, since the high inflation figures registered in the fourth quarter of 1999 will be replaced by lower rates in the same period of 2000.

Probability of Triggering Consultation Mechanism (%)

Year	Q	Economic Program(IMF)			
		Outter Band			
			Inner Band		
1999	4	0.0	0.0	42.8	1.8
2000	1	9.8	25.3	27.7	11.1
2000	2	9.4	20.0	45.7	28.0
2000	3	12.8	22.8	48.8	33.8
2000	4	27.1	39.0	35.0	23.7

The table on the left shows the probabilities of triggering informal and formal consultations with the IMF (as far as the deviation of inflation in relation to the target surpasses +/- 1 or +/- 2 percentage points, respectively). Such probabilities are implicit in the inflation fan chart and are conditional on the model and on the baseline scenario. The warning mentioned in the previous paragraph reflects a high probability of an informal consultation with the IMF in the second and third quarters of 2000. These chances come close to 50% since the central projection is near to one percentage point above the value of the quarterly target in these two periods. The probability of a formal consultation to the IMF in the third quarter is around 34%.

Forecasted IPCA inflation from "Relatório de Inflação" - September 1999

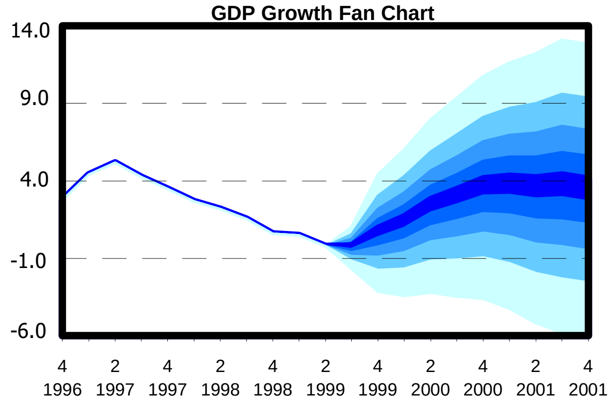


(acumulated inflation in 12 months)

When the current projection is compared to that of the September *Report*, republished here, a sharp increase of the inflation rate for the whole forecasting period can be observed. Firstly, this increase is due to the supply shocks that occurred in October and November 1999 and, although mentioned in the September *Report*, were not appropriately quantified. Besides, the current inflation fan chart is a result of a careful reassessment of the impacts of government managed prices and other changes in the baseline scenario.

The supply shocks already noted should raise the accumulated 1999 IPCA to 8.9% or 1.5 percentage points above the central projection in the September *Report*. Back then, it was 7.4% and included a built-in inflation expectation of 1.3% for the fourth quarter. In October and November, the IPCA increased by 2.15%, out of which 1.07% was due to only three items (new cars, beef and fuel alcohol). Excluding these items and assuming December inflation of 0.56%, as implicit in the current central projection, the IPCA would have increased by 7.7% in the year, well within the 30% confidence interval presented in the September *Report*. It is precisely the possibility of shocks of this nature and intensity what justifies the definition of targets with relatively broad tolerance bands. When working with a full price index, the figures do not always reflect the underlying process of price formation in the economy. Other countries that adopt inflation targeting regimes prefer to target an inflation index purged of typically seasonal or highly volatile items, with a narrower tolerance interval.

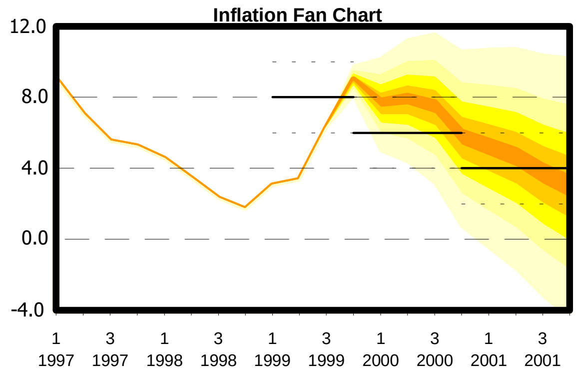
GDP growth with 19% p.y. fixed interest rate



(GDP variantion, 12 months over previous 12 months)

As in the previous *Report*, this issue shows the output growth fan chart constructed on the basis of the same hypotheses used in the baseline scenario. It should be stressed that the forecasting errors associated with GDP growth projections are considerably larger than the ones in the case of inflation projections. This is because GDP growth projections incorporate two non-observable components (potential output and output gap). Moreover, the estimation of output is, by definition, more complex and less precise than that of inflation. The central projection for output growth in 2000 is approximately 3.5%, assuming interest rate fixed at 19% p.a. for the year.

Forecasted IPCA-inflation with market interest rate 1/



(accumulated inflation in 12 months)

1/ In 12/16/1999 at 12:00 am

IPCA with market interest rate 1/

Year	Q	Confidence Intervals						Central Projection
		50%						
			30%					
				10%				
1999	4	8.6	8.7	8.9	9.0	9.1	9.3	8.9
2000	1	6.5	7.0	7.4	7.8	8.2	8.7	7.6
2000	2	6.4	7.0	7.5	8.1	8.6	9.2	7.8
2000	3	5.6	6.4	7.0	7.7	8.4	9.1	7.3
2000	4	3.6	4.5	5.3	6.0	6.8	7.7	5.6
2001	1	2.8	3.8	4.7	5.5	6.4	7.4	5.1
2001	2	2.0	3.1	4.1	5.0	6.0	7.1	4.5

Note: Accumulated inflation in 12 months, in % p.y. The values correspond to the shown in the inflation fan chart

1/ In 12/16/1999 at 12:00am

As an exercise, this issue presents the inflation fan chart taking into account the interest rates expected by the financial market on December 16th , a day after Copom decided to keep the basic interest rate at 19% p.a. The intention underlying the usage of the expectation a day after the Copom meeting is to capture the market reactions to the latest decision regarding the most important monetary policy instrument. The interest rate path expected by the market has a positive slope during the course of 2000, but is not sufficiently distant from 19% per year. Therefore, it shows a substantial change in the inflation fan chart. It should be stressed that, given a specific scenario, we cannot directly infer the impact of changes in nominal interest rates on the future inflation path (see Box Construction of Scenarios for the Inflation Fan Chart).

This *Report* also presents the Central Bank projections for other commonly used indices and compare them with market projection, representing the median of information obtained from approximately 70 financial institutions and

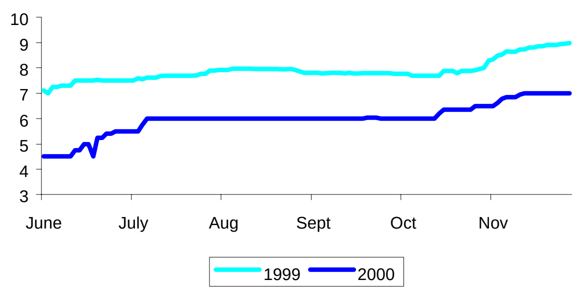
Other Inflation index projection

Index	Year	Confidence Interval						Central Projection	Market Projection 1/
		50%							
			30%						
				10%					
INPC	1999	7.6	7.9	8.1	8.3	8.6	8.8	8.2	8.2
	2000	2.7	3.7	4.6	5.4	6.3	7.3	5.0	6.5
IPC FIPE	1999	8.1	8.4	8.6	8.8	9.1	9.3	8.7	8.8
	2000	4.7	5.7	6.6	7.4	8.3	9.3	6.9	6.3
IGP-DI	1999	19.5	19.9	20.2	20.5	20.8	21.1	20.3	19.6
	2000	6.7	7.8	8.7	9.6	10.6	11.6	9.1	8.0
IGP-M	1999 2/	19.3	19.6	19.9	20.2	20.5	20.9	20.1	19.6
	2000	6.4	7.5	8.4	9.3	10.3	11.3	8.8	8.0

Note: Year over year under the assumption of 19% (fixed) interest rate
1/ Market perceptions (70 institution) 12/21/1999
2/ Projetion done in 12/21/1999

consulting firms. For this year, differences between the two median projections are irrelevant. For 2000, market analysts project a higher INPC and a lower IPC-Fipe. Regarding the general indices, the projections in this *Report* are higher than those expected by the surveyed institutions. However, market projections are well within the 50% confidence interval. When the projections in the last *Report* are compared to those in this, the figures for the year 2000 increase for all indices, particularly for the general ones, which are more affected by the evolution of wholesale prices.

Daily Evolution of Market's IPCA Forecast



The graph on the left shows the evolution of market expectations for the IPCA. After coinciding for several months with the inflation target for 2000, market projections have increased to 7% since late November. The 1 percentage point difference between projected and targeted inflation for next year is basically the same as for 1999.

Government Managed Prices

Analyzing what has occurred to prices up to November, it can be observed that the rate of inflation measured by the broad consumer price index (IPCA) came to 8.3%, at the same time in which government managed prices rose by 19.2%. Obviously, this leads to the question: Just what is a government managed price?

In Brazil, it is usually considered as a government managed prices those that, in one way or another, are defined or impacted by a public sector agency, independently of current supply and demand conditions. Several of these administered prices are IPCA components and have considerable weight in consumer spending. The major administered prices are listed below:

Prices defined at the municipal or state level:
Piped gas
Urban real estate and land taxes – IPTU
Vehicle license fees
Water and sewage fees
Public transportation, including urban and intercity bus, subway and taxi fares;

Prices defined at the federal level:
Oil byproducts, including gasoline, vehicle oil and cooking gas
Fuel alcohol
Residential electricity fees
Telephone and postal service fees
Public transportation, including air travel tickets and interstate bus service
Health plans and insurance.

Taken together, these components account for more than 25% of the total index, thus mirroring their importance in the overall daily outlays of households in the income bracket from one to forty minimum wages. At this point, we will present an analysis of the setting of some of these government managed prices at the federal level.

The prices of oil byproducts are determined according to the terms of Law No. 9,478, dated 8.6.97, known as the Petroleum Act. Since July 1998, the price structure has encompassed three basic components: the wholesale price, the reference price at Petrobrás oil plants and the specific price component (PPE). The wholesale price is the sale price charged to distribution companies and is determined in joint ministerial orders issued by the Ministry of Mines and Energy and the Ministry of Finance. The reference price is usually altered monthly as a function of changes in international market prices for similar petroleum products derivatives. Finally, the PPE, which is the difference between the wholesale and the reference price, defines the financial relationship between Petrobrás and its controlling shareholder, the National Treasury, in the so-called “petroleum account”.

Once derivatives have been sold to distribution companies, their prices are set freely in the intermediate stages from distribution companies to final consumers. These are the prices that are collected by the IPCA and other consumer price indices, while the wholesale price is taken as a component of the wholesale price index. In the first eleven months of this year, the IPCA was impacted by a 50.8% increase in gasoline prices, while the wholesale price was influenced by international market price hikes and rose 62.2%. The case of liquid petroleum gas was the same: the price increase borne by Petrobrás closed at 61.8%, while only 43.7% was passed through consumers (IPCA).

Electricity tariffs are determined according to contracts signed by concession companies and Aneel (Brazilian Electricity Regulatory Agency). The sector was subdivided into generation, transmission and distribution. Distribution is what really matters to consumers. In general, the contracts set an annual adjustment to be implemented at twelve month intervals. The rate adjustment takes account of two factors: the first covers only exogenous costs to the company (those over which the company has no control or negotiating power); and the second involves internal costs, indexed by the general price index – market (IGP-M).

It should be stressed that these contracts are subject to revision. A contract revision can be requested by the service provider and has the objective of ensuring its economic-financial equilibrium. In such cases, the components taken into consideration are productivity gains, cost and revenue structures, energy market conditions and price levels practiced by similar companies in Brazil. Rates can be revised upward or downward. Up to November 1999, the IPCA electrical energy component increased by 19.2%.

In the telecommunications sector, the maximum fees permitted are adjusted by Anatel (National Telecommunications Agency) on the basis of concession contracts. These adjustments consider changes in the general price index (IGP) and productivity gains, which normally vary from one service provider to another and from one service category to another. The telecommunications components in the IPCA reflect the costs of fixed telephone service and, more recently, mobile cell phone service. The rate increase from January to November came to 8.8%. However, as a consequence of market competition, companies do not always charge the maximum allowed rates, explaining the fact that negative growth was registered in April and in the last three months of the year.

The process of adjusting and revising the prices of health plans and insurance is coordinated by the Ministry of Health. The Ministry analyzes proposals submitted individually by each operating company with details relating cost variations and service demands. In 1999, the IPCA pointed to an increase of 7.9% in health plans and insurance.

In summary, the 19.2% increase in administered prices in 1999 accounted for a major share of the inflation measured by the IPCA. On the other hand, the prices of tradable goods increased by 9.4%, as they are directly impacted by changes in the exchange rate. As for the prices of nontradable goods and services, the increase was just 1.5%.

For the year 2000, administered prices are not expected to exert such a significant impact on inflation. As mentioned, the rise in oil byproduct prices, resulting from an extraordinary upward spiral in international market prices, was the single most important source of increase in the cost of living. And there are no clear expectations of additional price rises in 2000. Should international prices stabilize in the range of US$ 20.00 per barrel for Brent-type petroleum, current domestic prices for oil byproducts will not have to be altered.

Compliance will be demanded with each at every one of the clauses in contract clauses involving public utility services. Since 1996, telephone and electricity tariffs have increased at a rate higher than inflation. These increases were the result of realignment and elimination of cross subsidies which were aimed at moving prices into a range compatible with the providing of efficient services with attractive earnings on investments in both sectors. However, as the service providers are entitled to demand rate revisions whenever they conclude that their operations have shifted into a position of fundamental financial imbalance, the government may act through its regulatory agencies so that the terms of the concession contracts are fully complied with. Consumers of these essential services should not be forced into an equally financial imbalance. In this sense, it should be pointed out that ANEEL has recently denied a demand from eight service providers for an increase in their fees based upon financial unbalance.

The Construction of Scenarios for the Inflation fan Chart

The inflation fan charts presented in the *Report* are based on a path for the Selic interest rate, the basic Brazilian interest rate. However, in any macroeconomic model, projected inflation does not depend exclusively on interest rate but also considers several exogenous factors, that is, variables that are not determined by the dynamics of the model. Therefore, when building up scenarios, it is necessary not only to make assumptions on the path of the exogenous variables but also make such paths consistent with the assumed interest rate.

The scenarios are designed considering the available set of information on the domestic and international economies. Theoretically, one could construct an infinite number of scenarios based on a countless number of outcomes produced by the chosen variables. In practical terms, however, this exercise is limited to three to five scenarios. Among them, the one that Copom chooses as the most feasible (the basic scenario) is selected and guides the analyses in the Report, explaining monetary policy decisions.

It is essential to guarantee consistency among all the hypotheses in each scenario. To exemplify this, let's take a very simple model in which macroeconomic dynamics is simultaneously determined by an aggregate demand equation (IS curve) and a supply equation (Phillips curve). This model has four variables (inflation, the output gap, nominal interest rate and exchange rate) and just two equations. Of course, it is not possible to solve the system. As the major monetary policy instrument, the interest rate is clearly an exogenous variable. However, in a floating exchange rate system, the exchange rate cannot be considered exogenous. Thus, a parity condition is added in order to describe the exchange rate behavior in terms of the Brazil sovereign risk and the spread between domestic and international interest rates, both determined by exogenous factors in this example.

The next step is to establish different scenarios for the exogenous variables. One possibility is a constant external interest rate. As for the 'Brazil risk', it can be related to the current account results, to fiscal policy, international liquidity levels and shocks. If improvements are expected, based on prospective analysis, the 'Brazil risk' will follow a downward path. This scenario would be consistent with a dropping or constant interest rate, thus affecting both inflation and the output gap. A rising interest rate hypothesis makes no sense with falling external risk as higher interest rate would worsen the fiscal outlook and damage risk perception.

This example helps to understand why, when comparing the two inflation fan charts, it is not possible to state that the change in inflation trend is solely a result of interest rate moves, since the scenario has also been altered.

Exchange Rate Devaluation and Inflation

The literature on the relationship between exchange rates and price levels, or between nominal exchange rate devaluation and inflation has grown vigorously in recent years. The subject has gained prominence in face of two distinct phenomena. The first is the generalized inflation drop in the developed countries, particularly in the United States, whose robust performance has been marked by robust economic growth, record-low unemployment and low inflation. One of the factors that help explain this "puzzle" is the dollar appreciation. In this case, there is a deflationary impact of the exchange rate on prices. The second phenomenon is the departure from a fixed exchange rate system in unfavorable circumstances, as illustrated by the 1997 Asian crisis and the January 1999 devaluation of the Brazilian currency. In these cases, the impact of the exchange rate on prices is inflationary.

Despite having some points in common, the two phenomena are qualitatively different. In the first, the exchange rate is flexible, while in the second it is used as a nominal anchor. In this situation, a currency devaluation hits the economy as a considerable shock, due to its unexpectedness, to its generally high magnitude, or to the (at least) temporary loss of the economy's nominal anchor. The second situation will be analyzed with emphasis on the recent Brazilian experience.

At the beginning of the year, when the *real* was devalued in the midst of a severe currency crisis, most of the economists expected inflation to rise sharply, as had happened so often in the past. They feared that the stability obtained in the previous four and a half years at a high cost would vanish from one day to the next. To some extent, defense of pegged exchange rate was founded upon wariness that any devaluation would be offset by inflation, though the outcome of the Asian crisis had already refuted this argument. Just a few months after floating the currency, the initial predictions were shown to be wrong in both qualitative and quantitative terms.

More recently, several months after the new exchange rate regime was put in place, the return of inflation was once more trumpeted. The reason was the sharp increase in wholesale prices, fueled by the ongoing devaluation of the *real*, which created a wide gap between wholesale and consumer inflation in 1999. It was only a question of time before the wholesale increases would be passed through to retail prices, releasing the "repressed inflation" in the economy.

In fact, the analytical mistake underlying the predictions made at the start of the year, and the more recent ones, is the same. Any analysis of the relationship between the nominal exchange rate and inflation must necessarily begin with the definition of real exchange rate. Real exchange rate is a fundamental relative price in the economy and measures the price ratio of international goods to domestic goods. Traditionally, the real exchange rate is defined as **e =EP*/P**, in which **E** is the nominal exchange rate, **P*** is the level of international prices and **P** is the level of domestic prices.

The price of international goods can change as a consequence of two factors: an alteration in the nominal exchange rate and/or an alteration in its prices in foreign currency. The wholesale price index (WPI), which includes a greater proportion of tradable goods, is a proxy for the price level of international goods. The consumer price index (CPI), which measures the cost of living more precisely since it contains a greater proportion of nontradable goods, is a proxy for the prices of domestic goods.

This is the starting point for understanding why the real exchange rate appreciated after the Real Plan, leading to high trade balance deficits. The domestic inflation does not converge immediately to the external inflation when the exchange rate is determined. This is due to wage and price rigidity, which in turn can be caused by indexation or sluggish adjustment to inflation expectations. In the beginning of the Real Plan, the prices of domestic goods kept rising for some time. On the other hand, tradable goods prices soon stabilized, due to import competition allowed by trade liberalization. Thus, the real exchange rate appreciation was caused by the relative price adjustment, translated into CPI inflation much higher than WPI inflation.

Symmetrically, it would be expected that the price of tradable goods would grow faster than that of domestic goods after the currency devaluation. By definition, this would be necessary to offset the real overvaluation. It must be underlined that the real exchange rate is an endogenous variable and that any departure from the equilibrium value would eventually vanish over the course of time. This process was already under way: in 1998, despite the fact that the nominal exchange rate was devalued by approximately 7%, CPI inflation in the city of *São Paulo* was -2% (a deflation).

There is considerable empirical evidence regarding currency devaluations in both emerging and developed economies. On examining the factors that could explain the magnitude of the pass-through to domestic inflation, the literature suggests the following: the pass-through coefficient is inversely proportional to the degree of appreciation of the real exchange rate at the moment prior to the currency devaluation, and is directly proportional to initial inflation level.

Annex

Minutes of the 39th Meeting of the Banco Central do Brasil Monetary Policy Committee (Copom)

Date: 09.22.1999
Place: 8TH floor meeting room Banco Central headquarters – Brasília – DF
Called to order: 5:55 PM
Adjourned: 9:05 PM

In attendance:
Members of the Board
Armínio Fraga Neto – Governor
Carlos Eduardo de Freitas
Daniel Luiz Gleizer
Edison Bernardes dos Santos
Luiz Fernando Figueiredo
Sérgio Darcy da Silva Alves
Sérgio Ribeiro da Costa Werlang

Department Heads:
Altamir Lopes –Department of Economics **(Depec)**
Carlos Yoshitaka Urata – International Reserve Operations Department **(Depin)**
Luís Gustavo da Matta Machado – Department of Banking Operations **(Deban)**
Alexandre Antonio Tombini – Research Department **(Depep)**
Eduardo Hitiro Nakao – Open Market Operations Department **(Demab)**

Other participants:
Alexandre Pundek Rocha – Senior Advisor to the Board and Executive Secretary of Copom
Cláudia Safatle – Press Advisor **(Asimp)**

The Board analyzed the recent evolution and outlook for the Brazilian and international economies in the framework of the recently adopted inflation targeting regime.

Economic policy measures

Measures related to financial system and credit market

Resolution no. 2,627, dated 8.2.99 - regulated constitution and operation of companies designed to provide credit to micro-entrepreneurs, an area in which demand is concentrated in small scale operations. This measure is expected to contribute to reductions in the rates normally imposed on this segment, while increasing the availability of funding and reducing credit risk in contrast to the system prior to issue of this norm, in which operations were highly informal and, for this very reason, risk to the supplier of the credit was much higher.

Circular no. 2,927, dated 9.8.99 - reduced the compulsory reserve rate on demand deposits and deposits subject to notification from 75% to 65%. This measure has the dual purpose of reducing the differential between the lending and borrowing rates of the national financial system, while expanding the volume of available credit.

Resolution no. 2,653, dated 9.23.99 - determined that total credit operations with the public sector would be restricted to 45% of adjusted net worth (PLA) by financial institutions, with an overall value of R$ 600 million for new operations. The previous norm (Resolution no. 2,461, dated 12.26.97) set the ceiling on credit to the public sector according to the balance of operations in effect in September 1997 indexed by 80% of the reference rate (TR). The goal of this alteration is to take a more flexible approach to the conditioning of credit operations. The underlying reason for the change in question is the current situation of financial balance found in several states and municipalities.

Circular no. 2,934, dated 10.4.99 - reduced the risk weighting factor from 100% to 0% applicable to credit operations guarantied by funds designed to share the risk of credit channeled to microbusinesses and small size companies. Adoption of this measure is aimed at creating conditions for expanding credit to this market segment through increased financial institution leverage.

Ministry of Finance Directive no. 377, dated 10.4.99 - reduced the financial operations tax - IOF rate from 1.5% to 0.5% on credit operations in amounts equal to or less than R$ 30 thousand, when the borrower is a legal entity subject to the special tax system applicable to microbusinesses and small scale companies.

Ministry of Finance Directive no. 385, dated 10.14.99 - reduced the IOF rate on credit operations with individuals from 6% to 1.5%, making the rate equal to that levied on operations with businesses, with the exception of those related to Directive no. 377, dated 10.4.99.

Law no. 9,872, dated 11.23.99 - instituted the Endorsement Fund for Employment and Income Generation, which will operate with funding drawn from the Worker Support Fund. The purpose of this Fund is to provide endorsements to credit operations under the terms of the Program of Employment and Income Generation (Proger).

Resolution no. 2,655, dated 10.5.99 - determined more favorable conditions for working capital loan operations carried out by Banco do Brasil and the Federal Savings Bank, with funding from the PIS/Pasep Participation Fund. The beneficiaries are to be national companies and, preferably, micro, small and medium businesses involved in industrial, commercial and service activities, as well as individuals and legal entities that are beneficiaries of financing granted by micro-entrepreneur credit companies.

Circulars no. 2,925, dated 9.2.99 and no. 2,939, dated 10.14.99 - reduced the rate of compulsory reserves on time deposits, exchange acceptance funding, debentures and liability assumption contracts earmarked to operations abroad, from 20% to 0%. The objective is to create the conditions required to reduce the banking spread and increase the supply of available credit.

Provisional Measure no. 1,925, dated 10.14.99 - created the Bank Credit Bill, characterized as a credit security issued by individuals or legal entities in the benefit of a financial institution or equivalent entity, as a cash payment commitment generated by a credit operation and representative of a callable, liquid and firm cash debt. The purpose of this bill is to facilitate judicial execution of credits in litigation and reduce risk to the party granting the credit.

Circular no. 2,938, dated 10.14.99 - reduced the minimum value for Central Risk System registration by financial institutions involving debts for which their clients are liable, from R$ 50 thousand to R$ 20 thousand. The purpose of this measure is to reduce credit market risk, permitting the contracting of operations with a lesser differential between the lending and borrowing interest rates of the financial system.

Circular no. 2,941, dated 10.14.99 - altered Circular no. 2,910, dated 7.14.99, reducing the compulsory reserve requirements from 15% to 0% over liabilities for exchange purchases and advances in domestic currency, after discounting advances over axchange contracts.

Fiscal policy measures

Law no. 9,841, dated 10.5.99 - Instituted the microbusiness and small scale company law dealing with differentiated and simplified legal treatment in the administrative, tax, social security, labor, credit and business development fields, in keeping with the terms of Law no. 9,317, dated 12.5.96.

Provisional Measure no. 1,924, dated 10.7.99 - Introduced the following alterations into income tax legislation.

a. increase in the rate on remittances of interest on loans contracted abroad from zero to 15%, effective as of 1.1.2000;
b. increase in the rate on gains in variable income operations from 10% to 15% as of 2000 and to 20% as of 2001.

Law no. 9,876, dated 11.26.99 - Altered the calculation of retirement benefits of private sector workers and created the social security factor.

Provisional Measure no. 1,858-10, dated 10.26.99 - Maintained the rate of the Social Contribution on Net Profits (CSLL) at 12% up to 1.31.2000 and set the rate at 9% for the period from 2.1.2000 to 12.31.2002. According to the previous legislation, the 12% rate was to remain in effect until 12.31.99, dropping to 8% as of 1.1.2000. The Provisional Measure also determined that, as of 1.1.2000, legal entities would no longer be permitted to offset up to one third of the effectively paid Cofins with the CSLL due in each period of quarterly or annual calculation.

Provisional Measure no. 1,923-1, dated 4.14.99 - Instituted the Fiscal Recovery Program aimed at fostering normalization of federal government credits referring to debts held by legal entities and consequent upon taxes and contributions managed by the Secretariat of Federal Revenue and National Social Security Institute, as a result of generating facts that occurred up to 8.31.99. The consolidated debts are subject to interest corresponding to the long-term interest rate and any other additions to such debts are explicitly prohibited.

Foreign sector policy measures

Circular no. 2,926, dated 9.2.99 - Altered the period of liquidation of financial exchange operations to 60 days, except in the case of purchase operations that are not subject to Firce registration. Such operations are to be contracted for immediate liquidation. Operations with variable income securities (stocks) should be liquidated in up to three business days after contracting.

Resolution no. 2,644, dated 9.10.99 - Permitted the opening and operation of foreign currency accounts at banks authorized to operate in the country, when such accounts are in the name of companies charged with implementing and developing projects related to the petroleum or natural gas productive cycle and electric energy transmission and generation.

Circular no. 2,944, dated 10.21.99 - Altered the regulations on export exchange operations in such a way as to include operations backed by export credit insurance, permitting the extension of the exchange contract liquidation term for an additional 180 days.

Circular no. 2,947, dated 10.28.99 - Eliminated the ceiling on the exchange sold position of banks authorized to operate on the exchange market. The measure determined that such banks should effect deposits at Banco Central of the amount in excess of a bought position of US$ 6 million, for banks that operate in the free and floating rate markets, and US$ 1 million for those that operate solely on the floating rate market.

Resolution no. 2,664, dated 10.28.99 - Determined that banks should calculate their exchange positions upon terminating daily purchase and sale operations, encompassing all currencies and all of the institution's offices in the country.

Circular no. 2,948, dated 10.28.99 - Eliminated the demand for the prior contracting of exchange in import payment operations referring to Import Declarations (DI) registered as of 10.30.99.

Resolution no. 2,667, dated 11.19.99 - Determined that, for purposes of exports of aircraft to be used in regional aviation, the interest rate equalization of financing granted by Proex will use as its principal reference the United States T-Bond, plus a spread of 0.2% per year.

APPENDIX

Banco Central do Brasil Management

Members of the Monetary Policy Committee (Copom)

Banco Central do Brasil Management

Board

Armínio Fraga Neto
Governor

Carlos Eduardo de Freitas
Deputy Governor

Daniel Luiz Gleizer
Deputy Governor

Edison Bernardes dos Santos
Deputy Governor

Luiz Fernando Figueiredo
Deputy Governor

Sérgio Darcy da Silva Alves
Deputy Governor

Sérgio Ribeiro da Costa Werlang
Deputy Governor

Members of the Monetary Policy Committee (Copom)

Voting members

Armínio Fraga Neto
Governor

Carlos Eduardo de Freitas
Deputy Governor

Daniel Luiz Gleizer
Deputy Governor

Edison Bernardes dos Santos
Deputy Governor

Luiz Fernando Figueiredo
Deputy Governor

Sérgio Darcy da Silva Alves
Deputy Governor

Sérgio Ribeiro da Costa Werlang
Deputy Governor

Non-voting members

Alexandre Pundek Rocha
Board of Directors Consultant

Alexandre Antonio Tombini
Head of the Research Department (Depep)

Altamir Lopes
Head of the Department of Economics (Depec)

Daso Maranhão Coimbra
Head of the Department of International Reserve Operations (Depin)

Eduardo Hitiro Nakao
Head of the Department of Open Market Operations (Demab)

Luis Gustavo da Matta Machado
Head of the Department of Banking Operations (Deban)