THE NEW BRAZIL PLAN

Governo do Brasil

The New Brazil Plan

Federative Republic of Brazil

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The present document contains a brief description of the main initiatives which comprise The New Brazil Plan, launched by President Fernando Collor de Mello on March 16, 1990. It does not cover the whole set of measures taken by the Brazilian Government since its inauguration. The purpose of the document is to present an overall picture of the significant process of change which is now taking place in the Brazilian Economy.

The Brazilian Economy Prior to March 1990

The Brazilian Economy before March this year was visibly disorganized. Inflation was increasing at alarming rates (72.8% in February), while industrial production was shrinking. The Gross Domestic Product for this year was expected to fall as the high level of uncertainty amongst the country's economic agents was reflected in a drop in the investment rate, normally 20% in the seventies, to below 17% in 1989. A burgeoning public deficit, together with a generalized system of indexation of prices, wages and financial assets, forced the Central Bank to adopt a passive monetary policy, which, in turn, refueled the inflationary process. Protectionist pratices and the resulting lack of foreign competition reduced the efficiency of domestic production, in general.

The New Brazil Plan was launched by President Fernando Collor on the very first day of its Administration. The Plan combines a stabilization program, leading to a sharp decline in inflationary rates, with a set of structural reforms aimed at increasing the productivity of the economy, the modernization of the State, the opening of the economy to foreing trade and investment, and the deregulation of domestic markets.

Inflation Control

Significant advances were made to control inflation, which is now around 10% a month. Contrary to what happened in past stabilization programs, when most prices were frozen by the Government, the reduction in the rate of inflation is now taking place in an environment where only an extremely small number of essential goods have their prices still under control. The Government is determined to maintain the efforts made to so far since financial stability is a pre-condition for the resumption of growth trough private investments, both local and foreign.

The Fiscal Policy

The fiscal policies of the Government is one the mainstays of the adjustment program. The National Treasury accounts have shown positive results every month since the Government took office with an accumulated surplus in the last six months corresponding to Cr$ 335 billions, compared to a deficit of Cr$ 230 billions in the first quarter. The Central Government's fiscal revenues from January to August grew by 57% in real terms, while expenditures fell 7% also in real terms.

The budget for 1990 envisages for the first time in many years a positive result, with a surplus of some 1.22% of GDP in the Government's accounts. This represents a fiscal adjustment on the order of 10% of GDP. The results so far achieved derive from a broad program of adjustment, quite distinct from the ones applied is previous years, when it was expected that significant improvements could be made by introducing selective cuts in public spending. This time measures have been taken to increase tax income, reduce the States' financial commitments and diminish expenses with personnel. In short, only a program of consistent and courageous measures could engender the transformation the country required.

The Monetary Policy

The Government's monetary policy is of an unprecedented nature. Immediately after the economic program was launched, liquidity in the economy was drastically reduced. The explosive growth in money supply observed in the beginning of the year was reversed; inflationary expectations began to recede, as reflected by the fall of nominal interest rates; the trade balance is back to satisfactory levels, reflecting the exporters' confidence in the new Government's exchange policy.

Since May 1990, after the remonetization stage was completed, the Central Bank began to operate an active monetary policy and to exert effective control on the money supply. This policy was introduced when the decision was taken to stop financing the federal bond portfolios held by financial institutions.

For the second half of this year, the National Monetary Council authorized expansion targets of 9.1% for M1 and 11.2% for M4. To give an idea of the size of the adjustment that these targets represent, it should be recalled that expansion in M1 and M4 in the first half were 1,033% and 214,5% respectively. For the first quarter of 1991, growth in both M1 and M4 will be zero per cent.

The Exchange Policy

The Exchange policy was radically altered by the introduction of floating exchange rates freely set by the market, replacing the previous system of daily rates fixed by the Central Bank.

The remission abroad of profits, dividends and returns has been freed from controls, where they previously had to go on deposit in the Central Bank.

Financial institutions have been authorized to obtain funding abroad by issuing commercial papers, making the resources available to domestic borrowers.

The Administrative Reform

The Government is determined to achieve a significant reduction in employment in the federal public sector, which includes the central administration, public enterprises, official banks and federal agencies. By mid August some 145.000 civil servants had been dismissed, and 43.000 had put on an availability status. All vacancies in the civil service are frozen and a retraining program has been prepared to facilitate the recycling of personnel on availability status within federal bureaucracy.

Furthermore, several Government agencies have been extinct. The number of Ministries has decreased from 23 to 12.

Privatization

The Government has launched an ambitious privatization program that is designed to free fiscal resources and to promote efficiency gains in the economy. The first group of public firms to be privatized within the next three years includes ten firms in the steel, petrochemical and fertilizer sectors, the total worth of which is preliminarily estimated to reach US$ 15 billions on a net basis. Besides these enterprises, the

Government is selling its minority participation in 16 other firms in the petrochemical sector. Revenues from privatization will be used to repurchase public debt. Financial institutions will be required to acquire privatization certificates, which will be applied to the purchase of stock in the public enterprises to be privatized. The certificates will facilitate the sale of public enterprises and ensure a minimum pace of privatization.

The New Trade Policy

All direct export subsidies have been eliminated. As regards imports, a complete overhaul was introduced. The two pervasive quantitative restrictions – a prohibition list of 1200 items and import company quotas – were eliminated, and tariffs were reinstated in its central role in determining the level of domestic protection. In addition, a tariff reform is under way to phase out by 1994 the average tariff rate to 20%, down from the current 37%. Import permits are now automatically issued within 5 working days. In short, the new imports policy is transparent, reliable and predictable. Besides, Brazil will no longer set trade surplus goals and restrict imports to attain those goals. As Brazil wants to increase trade both ways, trade surpluses would rather come as a consequence of our competitiveness in the world market.

The New Industrial Policy

The new industrial policy represents a departure from the import substitution model which was no longer compatible with Brazil's economic needs. It provides the private sector with a time horizon and clear directives as to changes to be introduced in the economy in the next few years. The targets, in broad terms, are trade liberalization, increased efficiency, and free competition.

Its main strategies are:

– Progressive reduction in the levels of protectionism;

– Enhancement of industrial competitiveness through the use of coordinated instruments of credit support to improve technological infrastructure;

– Strengthening of industrial sectors through greater specialization.

Anachronistic sectorial restrictions to foreign capital are to be eliminated. A new legal treatment to them is to be enacted. Direct investments will be of major importance to the country in this new phase.

Two main programs were started: a) the Industrial Competitiveness Program (ICP), which relates to the development of advanced technology sectors; and b) the Quality and Productivity Program (QPP), that provides for cooperation between the Government and the private sector and includes the following subprograms: incentives for industrial productivity; development and diffusion of management methods; human resources development; adequacy of technological services to quality and productivity.

The New Policy for Science and Technology

The strategy for the technological development of industry will have the enterprises themselves as its main agents. Loans and incentives will be directed to the private sector, which in turn will be encouraged to resort to universities and research institutes.

Investments in science and technology will increase from 0.8% of GDP to 1.3% of GDP in 1994. At last 2/3 of the additional resources will be invested in technology and 1/3 in science.

The private sector will increase its share of investments in science and technology from 0.03% to 0.17% of the GDP by 1994, representing an average growth of 35% per annum.

Federal credit agencies will conduct their operations in such a way that loans for the technological development of companies will increase from 3% of the total at present to 28% by 1994.

Rules applying to technology transfer contracts have been considerably simplified.

Digital Electronics and Data Systems

Important advances have been introduced in the legislation regarding the electronics sector. The basic objective is to promote the technological development of local companies throwgh a planned opening of the market, a revision of current restrictions on associations with foreign companies, and the introduction of a greater degree of flexibility in the local controls on production. The following measures were taken:

– revision of the legislation on data processing and digital electronics (known as the Informatics Law), with the elimination of certain clauses such as the one that defines *national* companies as those that have at least 70% of their capital in Brazilian hands and no more than 30% owned by foreign interests;

– new rules for importing and manufacturing data processing equipment. Until 1992, controls will only be maintained on imports of products in which local industry is considered competitive, with the decision as to what is competitive being taken by the National

Informatics Council on the basis of criteria that establish limits of tolerance for technological and quality gaps vis-à-vis competing foreign products, as well as for price differences between locally manufactured protected equipment and international market levels;

– the import tax on raw materials, components and parts for computers that come from other sectors of industry is to be reduced within a month;

– joint ventures with foreign companies that transfer technology will be permitted;

– in October 1990, the Brazilian Government will propose to Congress the revision of the Software law. Among the new rules that the Executive plans to suggest are the elimination of legislation prohibiting foreign programs from being marketed if similar local products are domestically produced, and the end to exclusive rights to market a particular software in the country.

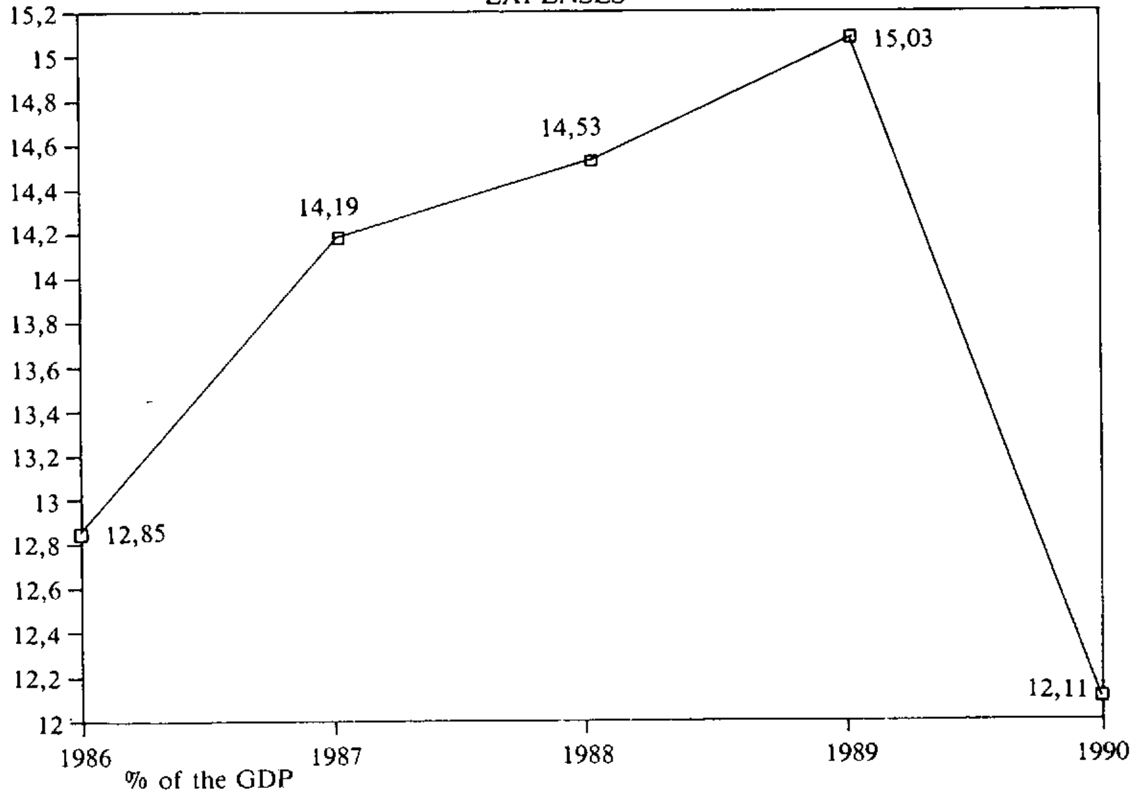
Foreign Debt

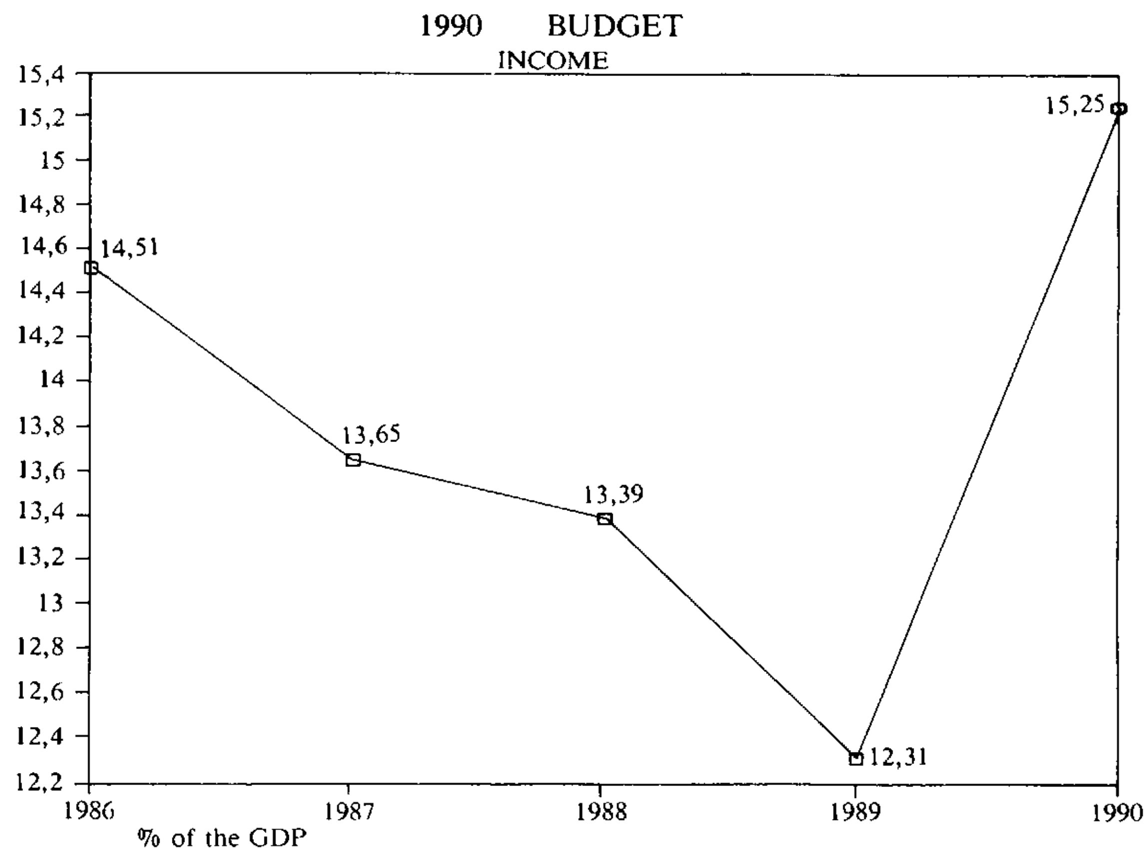
The solution of the foreign debt issue is crucial for the success of the economic program. Brazil is firmly determined to extricate itself from the vicious circle that has characterized the problem. We are prepared to enter into negotiations capable of bringing about lasting agrements. The Brazilian Government's stance in these negotiations will be guided by the need for strict matching of the debt service to the ability to pay, which is determined by fiscal and monetary constraints and must be consistent with macroeconomic equilibrium and sustained growth.

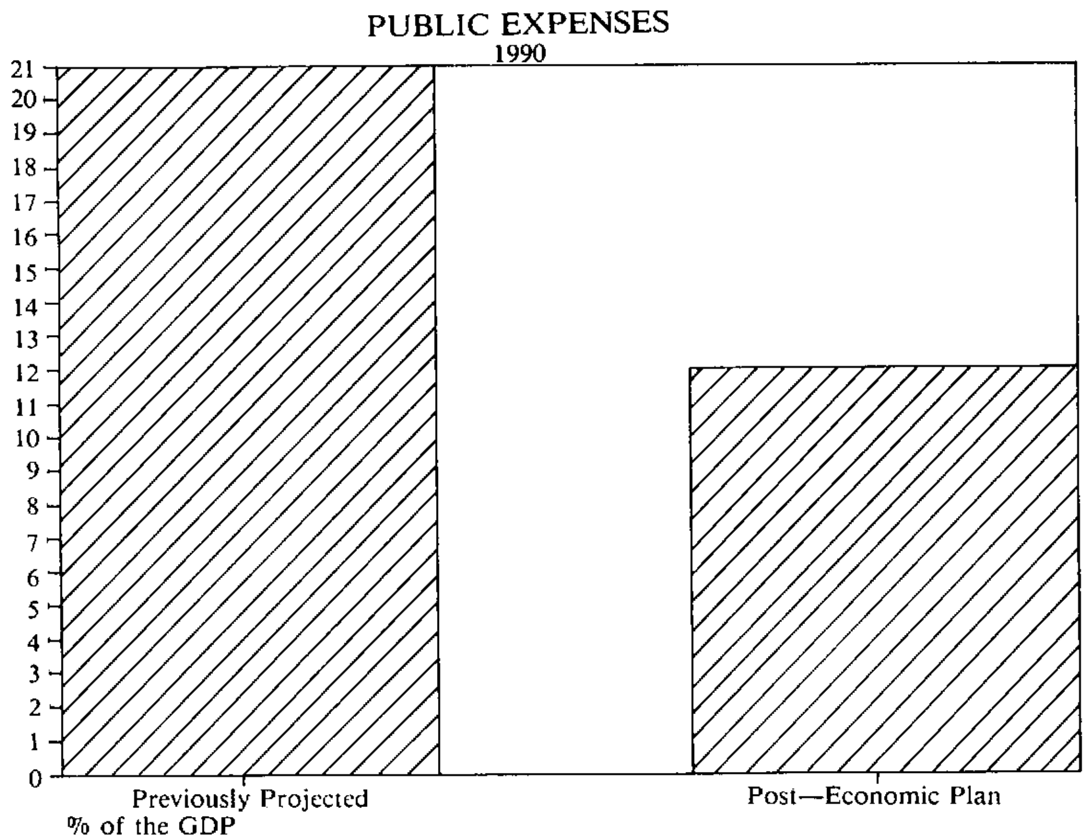
On September 13th, the Brazilian Government has sent a letter of intent to the International Monetary Fund. The acceptance of Brazil's adjustment program is an important factor, for it represents the Fund's recognition of the significant efforts being made to control inflation and resume growth.

We shall start in the first half of October negotiations with commercial banks. We shall also hold technical consultations with the Paris Club with a view to achieving positive results as soon as possible. The Brazilian Government approaches these negotiations in a spirit of cooperation. At the same time, Brazil is convinced that debt servicing should not give rise to pressures or jeopardize the country's legitimate need to promote economic growth.

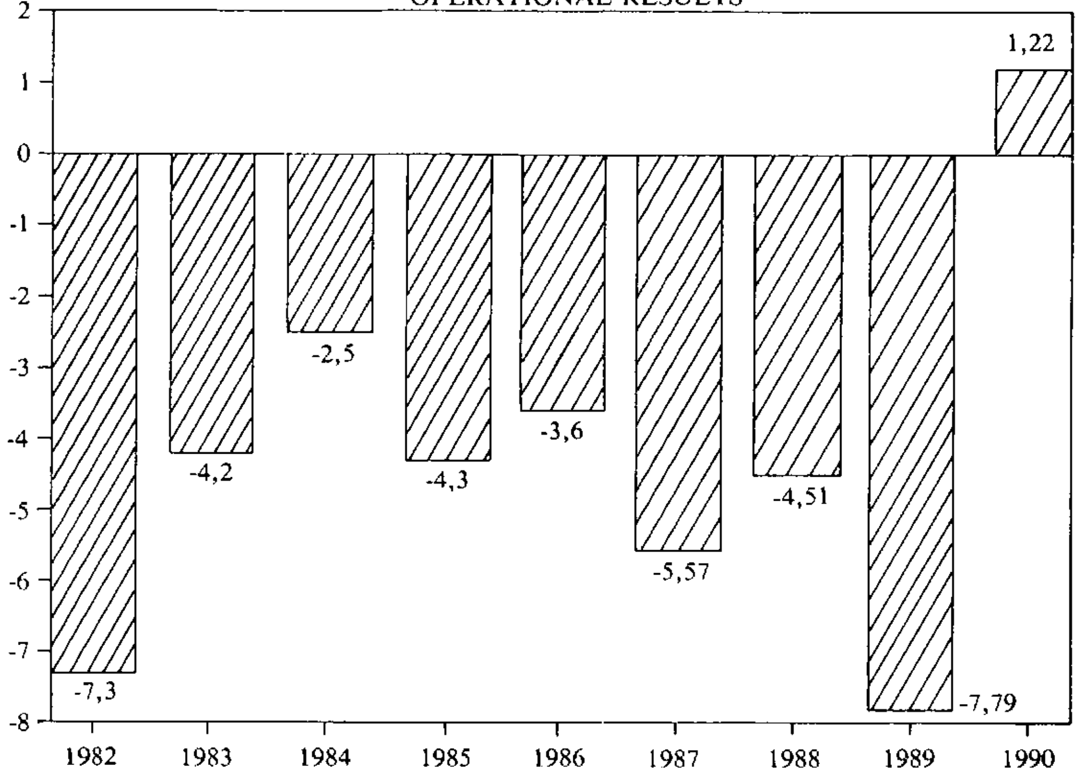
1990 BUDGET
EXPENSES




1990 BUDGET
INCOME
15,4
15,2
15
14,8
14,6
14,4
14,2
14
13,8
13,6
13,4
13,2
13
12,8
12,6
12,4
12,2
14,51
13,65
13,39
12,31
15,25
1986
1987
1988
1989
1990
% of the GDP


PUBLIC EXPENSES
1990
21
20
19
18
17
16
15
14
13
12
11
10
9
8
7
6
5
4
3
2
1
0
Previously Projected
Post—Economic Plan
% of the GDP

PUBLIC SECTOR
OPERATIONAL RESULTS

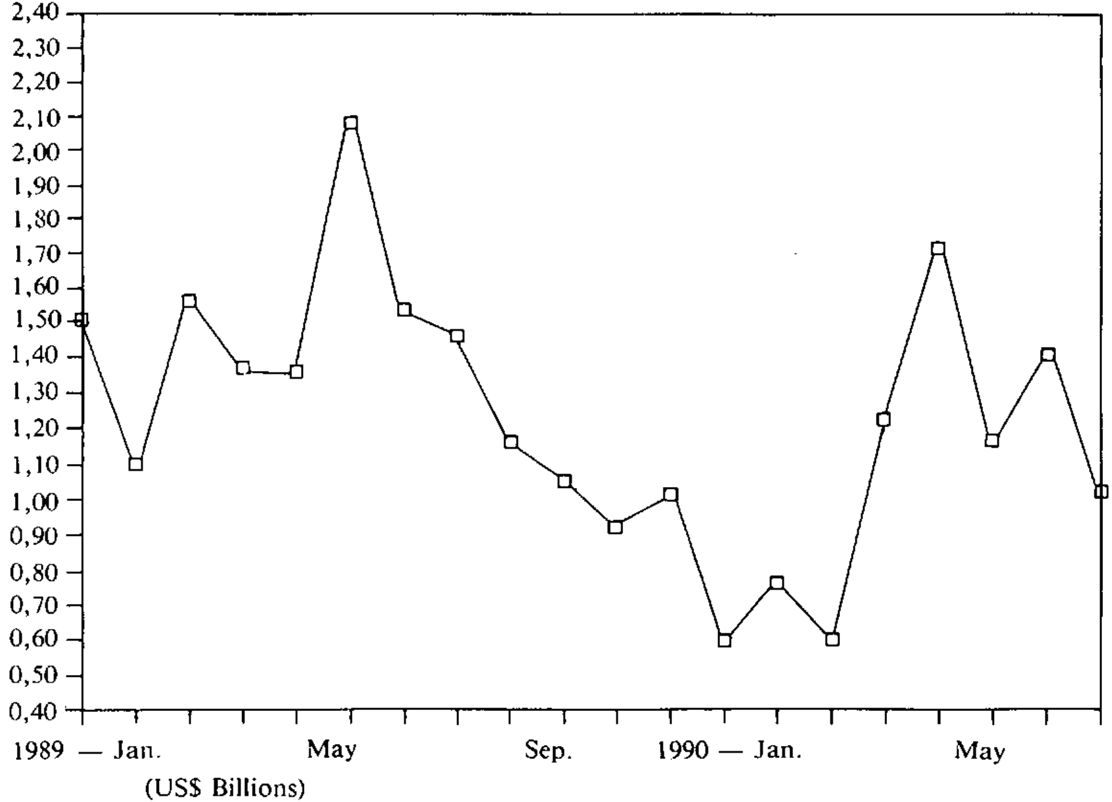


TRADE BALANCE

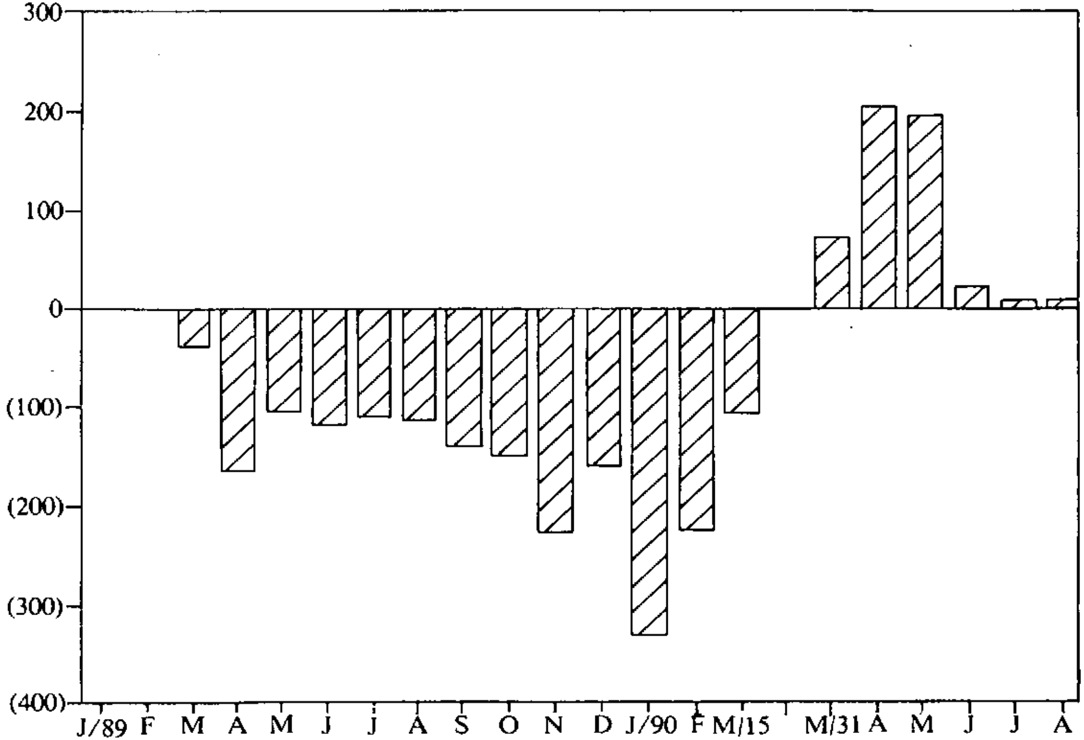
	Exports (US$ millions)	Imports (US$ millions)	Balance (US$ millions)
1989 – Jan.	2,751	1,236	1,515
Feb.	2,263	1,164	1,099
Mar.	2,847	1,280	1,567
Apr.	2,399	1,030	1,369
May	2,832	1,480	1,352
Jun.	3,683	1,603	2,080
Jul.	3,217	1,680	1,537
Aug.	3,372	1,909	1,463
Sep.	2,950	1,790	1,160
Oct.	2,746	1,687	1,059
Nov.	2,576	1,653	923
Dec.	2,770	1,751	1,019
Total –	34,406	18,263	16,143
1990 – Jan.	2,282	1,678	604
Feb.	1,981	1,210	771
Mar.	2,237	1,636	601
Apr.	2,559	1,334	1,225
May	3,230	1,503	1,727
Jun.	2,525	1,352	1,173
Jul.	3,060	1,640	1,420
Aug.	3,043	2,009	1,034
Total –	20,917	12,362	8,555

Source: Central Bank of Brazil

TRADE SURPLUS

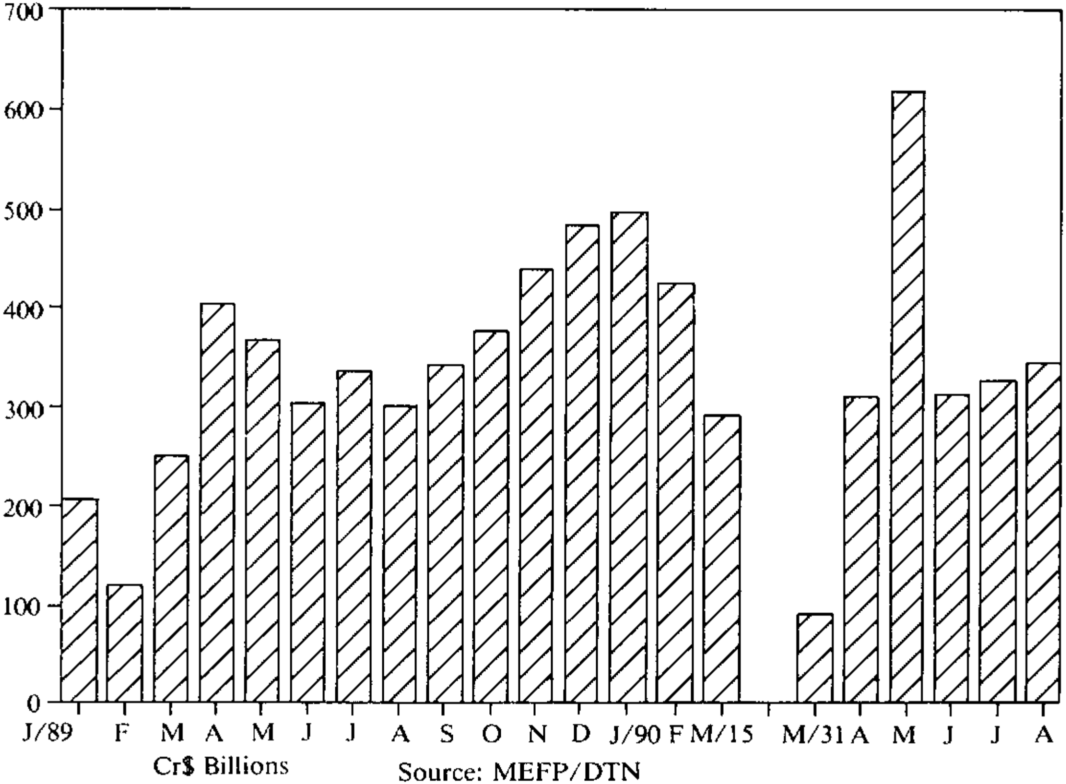


TREASURE ACCOUNTS



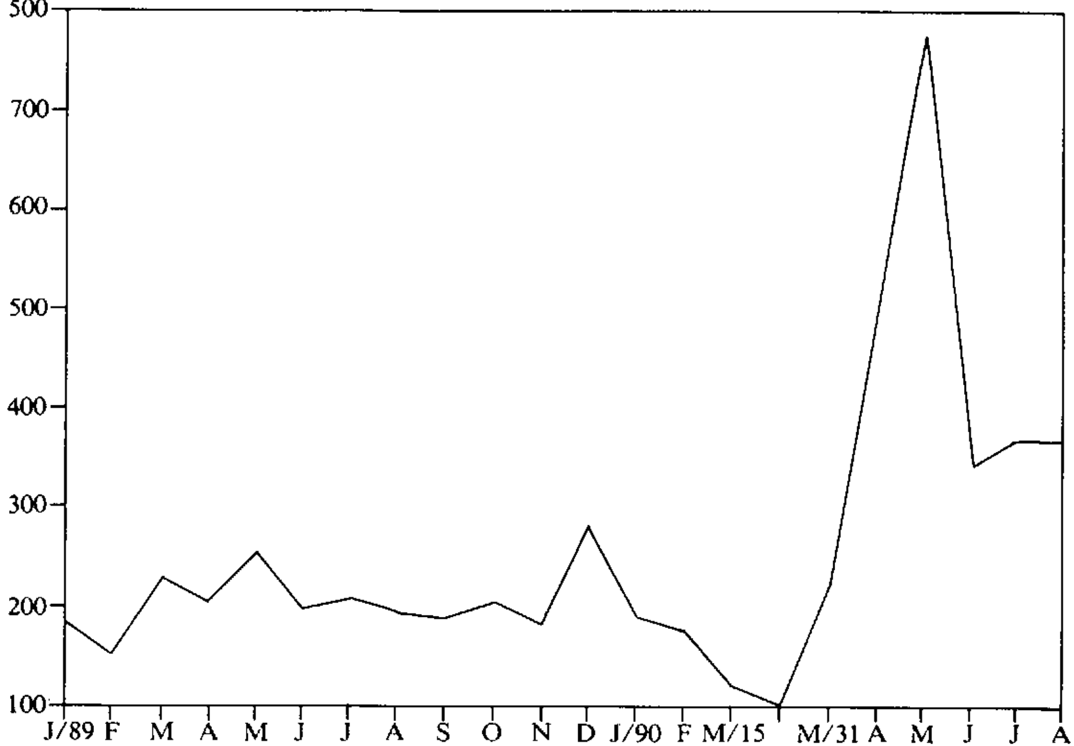
Cr$ Billions Source: Ministry of Economy, Finance and Planning

TREASURE ACCOUNT: FISCAL EXPENSES



Source: MEFP/DTN

FISCAL INCOME



Cr$ Billions

Source: MEFP/DTN

INFLATION RATES
Consumer Prices Index (IPC)

89		90		△ 90
Jan.	8,739	Jan.	213,028	68.19%
Feb.	10,168	Feb.	370,647	73.99%
Mar.	10,768	Mar.	523,650	41.28%
Apr.	11,636	Apr.	523,650	0.00%
May	13,575	May	551,822	5.38%
Jun.	17,567	Jun.	604,797	9.60%
Jul.	22,380	Jul.	670,055	10.79%
Aug.	29,806	Aug.	740,947	10.58%
Sep.	40,640			
Oct.	56,392			
Nov.	83,725			
Dec.	126,659			

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