



PRESIDÊNCIA DA REPÚBLICA
Governo Fernando Henrique Cardoso

**THREE YEARS
OF THE *REAL* PLAN
Building a Better Brazil**

BRASÍLIA
1997

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INTRODUCTION

What can we celebrate on the third anniversary of the *Real Plan*?

As each year passes, it is becoming clearer that the effects of the new currency were not limited to the drop in inflation and to the consequent increase in the population's purchasing power, and especially that of the lowest income groups.

Currency stabilization unleashed an intense transformation process that is changing the make-up of the country and bringing concrete gains to Brazilian producers and consumers, workers and businessmen, students and housewives, i.e., to all Brazilians.

Everything began, it is true, with the reorganization of the economy. Brazil returned to sustainable growth rates. From 1981 to 1993, per capita income had fallen by 5%; in the last three years, it has increased by 9% as a result of an average annual growth rate of 4.4%. This growth occurred simultaneously with a significant income transfer to consumers, and especially to lower income consumers. In July 1994, the basket of basic food items cost R\$106.95; in June 1997, it cost R\$112.03. Meanwhile, the average real income of workers increased by 22%.

The removal of economic uncertainties made it possible once again for consumers with low purchasing power to have access to credit. Thus, these consumers were able to buy more costly goods. Sales of electric appliances increased 66% from 1994 to 1997.

As a result of the effort to reorganize the public accounts, federal government social expenditures have increased 27%, in real terms, since the *Real Plan* was introduced. It is important not only to spend more, but also to spend more effectively. Through partnerships with the states, municipalities and even local communities, the implementation and supervision of many social programs are being decentralized. This

process is being applied in education, where resources are sent directly to the schools and are spent under the supervision of the Parent-Teachers Association (*Associação de Pais e Mestres*). In the health area also, more and more decisions are being left to the Health Councils (*Conselhos de Saúde*). Finally, in housing and sanitation, financing requests are approved after being reviewed by organs comprised of representatives from the public sector and from non-governmental organizations.

Because of these factors, Brazil today has fewer poor people. In 1994, the poor comprised 33% of the population in the principal metropolitan areas; last year they represented 25%. The degree of inequality in income distribution, although still high, declined.

The government created and is implementing the Brazil in Action Program (*Programa Brasil em Ação*) to promote the physical infrastructure and human resources necessary for investments. The privatization program that is now in progress and the constitutional amendments that are under review in Congress complete the framework of reforms necessary to assure growth in the coming decades.

As Brazil's economy is being restructured, its democratic system is being strengthened. The government welcomes society's desire to participate, and is stimulating this participation by decentralizing decision-making and control over a growing number of public-sector activities.

Democracy today represents also a daily struggle against violence and discrimination. The National Human Rights Program (*Programa Nacional dos Direitos Humanos*) affirms the commitment of Brazilian society and government to defend these rights. Lamentably, occasionally, the vestiges of a past that we would like to extinguish flare up and embarrass Brazil. However, the combined efforts of everyone are offsetting the impunity of those violent forces that infringe the rights of the unprotected.

These broad, profound transformations are rebuilding Brazil step by step.

Actually, the *Real Plan* initiated a broad movement to remove the chains that have impeded Brazil from realizing its potential: to build a truly representative and increasingly participatory democracy; to mobilize the human and physical resources needed to assure a sustainable growth rate capable of generating more jobs and better salaries; to promote a reform of the state and to focus the government's efforts where they are needed most; to redirect public services toward those who need them most in order to provide opportunities to those who never have had them, and who would have continued without them had it not been for the profound changes now taking place.

It is true that all this cannot be credited solely to the *Real Plan*. The changes that are taking place are, above all, the result of the determination and hard work of every Brazilian. However, it is also true that none of the significant gains would have occurred had it not been for the *Real Plan*, which finally succeeded in ending a cycle of economic disorganization, blunders and loss of self-esteem that characterized Brazilian society for more than a decade.

With the end of inflation, legitimate demands from different segments of society emerged with unquestionable vigor, broadening considerably Brazil's agenda. This trend is positive. However, the intensity of the demands bears no relationship to the ability of the society and of the government to respond. One cannot expect that long-standing problems, many of them centuries old, can be resolved overnight.

Relative to the past, much has been achieved. Relative to existing needs, much remains to be done. We know this. That is why we continue working, convinced that Brazil is back on course and that we are in a position to confront the country's extensive needs.

The scope of the work that lies ahead cannot prevent us from seeing that we have come a long way in a short time. The continued economic growth since 1994; an unprecedented redistribution of income; the emergence of a powerful consumer market; the return of productive investments; the effort to remove economic obstacles; and the gains that are already being felt in education, in health and in the improved living

conditions of the lowest income population are different aspects of the same reality: the redefinition of Brazil's development process.

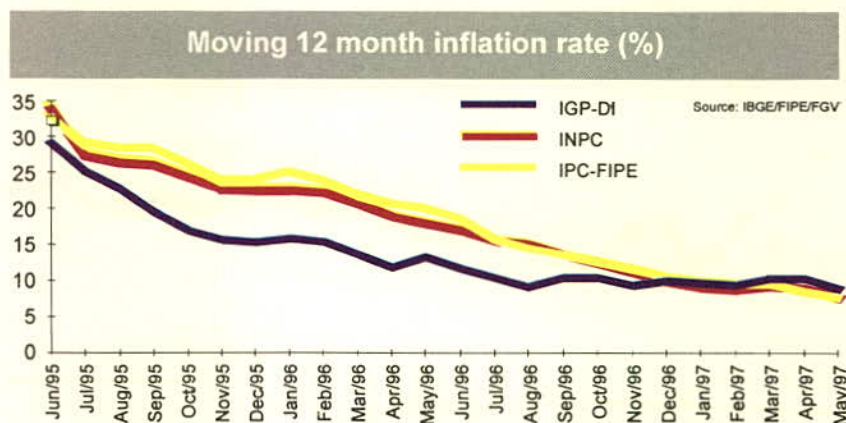
Gradually, Brazilians are regaining their self-confidence. They participate, they demand their rights, and they contribute to the new Brazil that we want to build. It is this partnership working for a better Brazil that we can celebrate on the third anniversary of the *Real Plan*.

Fernando Henrique Cardoso

I. CURRENCY STABILIZATION

The continued fall in inflation since the beginning of the *Real* Plan represents the greatest accomplishment of the Brazilian people in recent years. In the first half of 1994, consumer prices increased, on average, by more than 40% per month. In June 1995, the first anniversary of the *Real* Plan, accumulated inflation for the 12 months was 30%; by the Plan's second anniversary (June 1996), this annual percentage had been reduced to 15%. Now, after three years, Brazilians live with an annual inflation rate of about 8%.

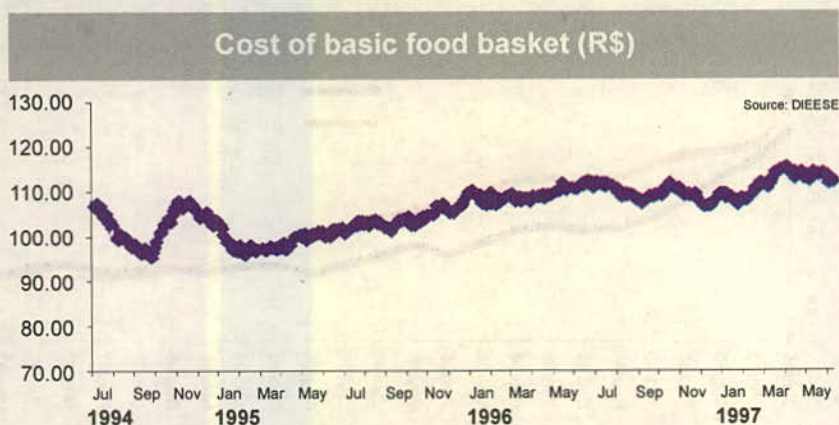
Monthly
inflation fell
from 40%
to 0.55%



It is well known that stability has benefited the entire country. Low inflation means that salaries maintain their purchasing power. This was not the case prior to the *Real* Plan. Even though salaries were readjusted each month, the velocity of price increases was always greater than that of the readjustments, thereby eating away the purchasing power of salaries. Low inflation brought a generalized change of attitude: indexation, which had been a perverse mechanism that automatically extended

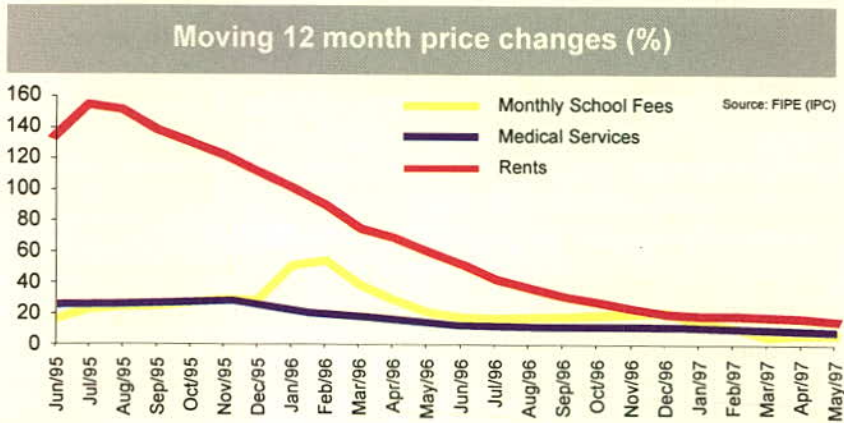
past inflation, is slowly disappearing from the population's daily lives. Those who had been least able to protect themselves against inflation (namely, those without bank accounts or means to invest in the financial market) are those who have benefited most from the end of indexation.

The lowest income segments of the population, therefore – without any doubt – enjoyed the most significant gains from the currency stabilization produced by the *Real Plan*. The change in the cost of the basket of basic food items in the last three years demonstrates this fact. On July 1, 1994, it costed R\$106.95; on June 11, 1997, it costed R\$112.03. This change represents an increase of less than 5% in 36 months. To illustrate, at the beginning of the *Real Plan*, more than 1.6 minimum salaries were needed to purchase a basket of basic food items; today, one minimum salary purchases a basket of basic food items and a little more.



Important changes have occurred in the structure of relative prices over the last three years. From the very beginning, with the opening of the economy, the prices of imported products were stable because of foreign competition. But the story was different in the service sector. Without the stabilizing effect of international prices, service prices increased initially in response to increased demand spurred by the currency stabilization. This was the case with rents, school tuitions and

medical fees. With the passage of time, prices of these services also adjusted and their fluctuations are converging toward the average rate of other prices. This is the good news. With all prices converging toward a lower rate of increase, not only food and clothing become part of the new world of stabilization, but also major items like school tuitions and rents cease to be the villains they were at the beginning of the *Real Plan* and become affordable to the consumer.



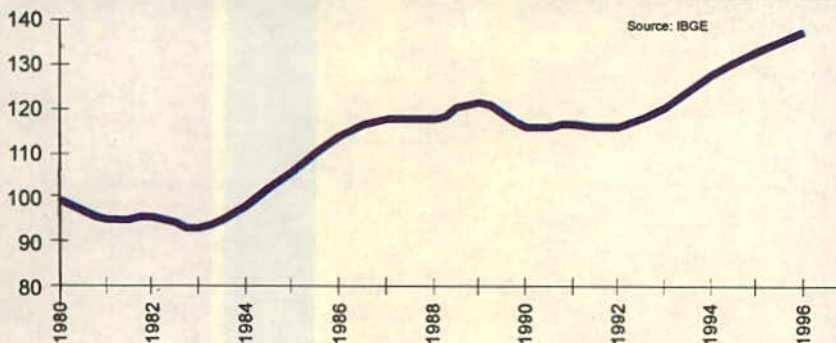
II. IMPACT ON THE ECONOMY

Growth

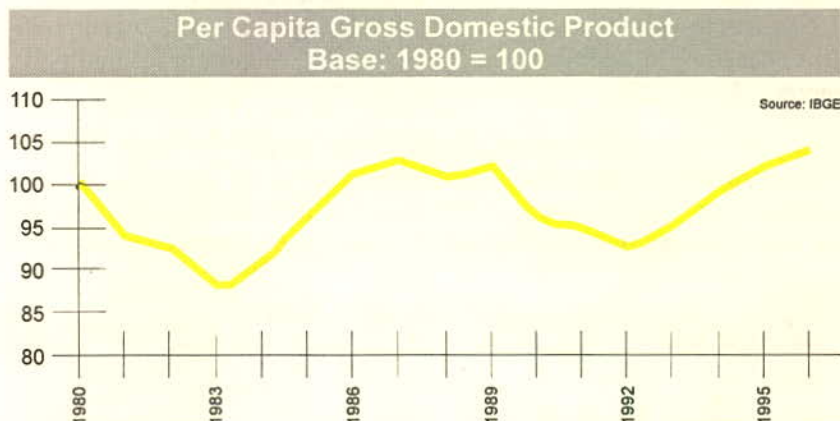
The Gross Domestic Product (GDP) has grown significantly throughout the period of the *Real Plan*: since the Plan's beginning in 1994, the accumulated growth has been 13.8%, which represents an average annual growth rate of 4.4%, compared to an average growth rate of 1.5% in the previous thirteen years (1981-93). More important than this growth is the fact that the annual rate of expansion has remained positive. This trend is contrary to the periods of accelerated expansion followed by substantial recessions that occurred in the 1980s and the beginning of the 1990s. The importance of this is not simply that we have been growing in recent years, but also that this constant growth has produced greater confidence in the Brazilian economy. This confidence is a fundamental element in attracting investments, which in turn further stimulate increased growth and employment.

The GDP grew 13.8% in the last three years, more than offsetting the decline in per capita income during the previous 13 years

Gross Domestic Product (GDP)
Base: 1980 = 100



As a result of this significant GDP growth in recent years, per capita GDP has also increased during the *Real Plan*. This increase is yet another indication of the improved quality of Brazilian life since the implementation of the *Real Plan*.



Per capita income fell by 5% during 1981-93. In only three years (1994-96), it was possible to reverse this decline of almost a decade and a half: per capita income grew by no less than 9%, which corresponds to an annual growth of 2.9% compared to an annual average decline of 0.4% in the previous 13 years.

Income Distribution

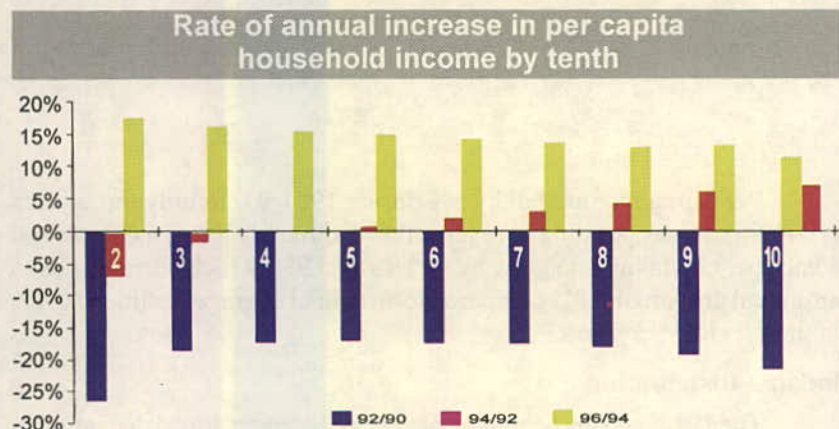
The 1980s and the beginning of the 1990s demonstrated that inflation reduced the income of the poorest members of society, whether due to their lack of access to the financial market or to the fact that salary readjustments, unlike monetary readjustments, never kept up with inflation. The rich, on the other hand, having access to "indexed" money (financial market assets that guaranteed not only a return to offset inflation, but also enormous gains on top of it), were able to protect themselves from inflation's corrosive effect and, often, to increase their share of national income.

The years 1994-96 registered an unprecedented phenomenon in Brazil's recent history: economic growth with income redistribution

Inflation, by increasing the inequality between the poor and the rich, became another factor that, along with recession and unemployment, explained the increase in poverty during this period.

The failure of the stabilization programs of the 1980s and early 1990s was the principal cause of the deepening of Brazil's social problems because, in addition to creating chronic economic instability, it increased inequality.

As can be observed in the following graph, the years 1994-96 registered an unprecedented phenomenon in Brazil's recent history: economic growth with income redistribution. All sectors enjoyed gains. However, the greatest gains occurred in the lowest income groups.



Therefore, the *Real Plan* facilitated significant reductions in poverty.

First of all, per capita income grew as the total wage bill rose 31% in real terms.

Secondly, the distribution of income improved, thanks to the end of the inflation tax that had fallen upon the poorest classes and to the increase in the real value of the minimum salary (21%). Moreover, the fluctuation of individual real incomes was reduced by 40%. This success contributed to greater confidence about future incomes and, therefore, a significant expansion in consumer credit.

Thus, poverty has recently been declining in Brazil. The percentage of poor in the population, which was 33.4% in 1994, fell to 27.8% in 1995 and to 25.1% in 1996. The share of income that goes to the poorest 50% of the population increased from 11.3% to 12.3%. Thus, the degree of inequality fell from 5.73 in 1994 to 5.13 in 1995 and to 5.07 in 1996¹.

**TREND IN INEQUALITY OF DEVELOPMENT
AND OF POVERTY – 1990-96 (%)
SIX MAIN METROPOLITAN AREAS**

	1994	1995	1996
Income share of the poorest 50%*	11.3	12.2	12.3
Income share of the richest 20%*	64.7	62.6	62.4
Degree of inequality	5.73	5.13	5.07
Per capita GDP growth	4.5	2.8	1.5
Percentage of poor*	33.4	27.8	25.1

(*) PME-IBGE Annual Averages – Earned Income.

Credit Availability

With stabilization, the financial system has begun to return to its principal activity: providing credit for production, trade and consumption. The resumption of credit operations by the financial institutions is another

Since stabilization, the financial system has begun to return to its principal activity: providing credit for production, trade and consumption

result of economic stabilization. In the period prior to the *Real Plan*, high inflation rates led the financial system to operate basically on a very short-term basis, creating mechanisms aimed at eliminating or reducing the losses caused by inflation. Access to such mechanisms was, for the most part, limited to the highest income segment of the population.

At that time, fixed installment payments for financing did not exist. Payments were always

(1) The degree of inequality is calculated as a ratio of the share of income of the richest 20% to the poorest 50%. In other words, the larger the share of income of the poor, the smaller the ratio.

being adjusted for inflation and, therefore, their future values were uncertain. Repayment terms were short and installments, consequently, were high.

With inflation under control, repayment terms are being extended; the elimination of monetary correction makes fixed installment payments possible.

With the resumption of credit operations, Brazilians can increase their consumption of more costly durable consumer goods (electric appliances, furniture, automobiles, etc.). The access of individuals to lines of credit increased their participation in the financial system.



The entry of foreign banks into Brazil, as well as the extensive restructuring of the domestic financial system, augments competition in the market, increases the security of those who use bank services, and contributes to reduce interest rates and bank fees. These are positive changes for the consumer.

Interest Rates

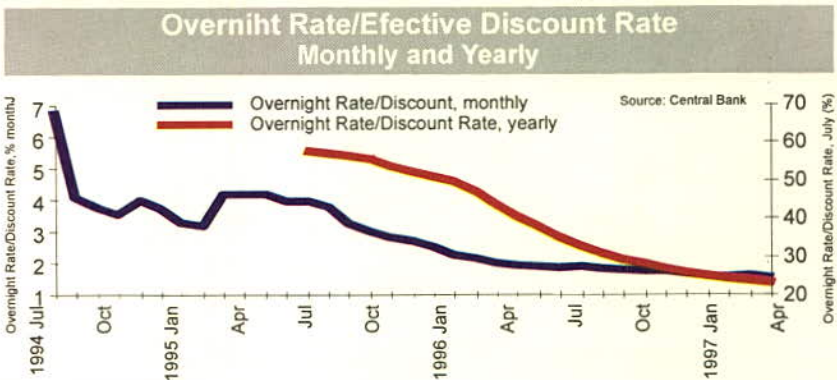
Despite remaining high in comparison to international standards, interest rates have been reduced concurrently with the fall of inflation. In July 1994, interest rates (overnight/discount) were 6.87%

per month, the equivalent of 122% in annual terms. By May 1997, using the same measure, the rate had fallen to 1.58% per month, or 23.79% during 12 months.

Although not yet comparable to world levels, the decline in interest rates speaks for itself

Ever lower interest rates will mean more consumption, more investment and, therefore, more employment. This is why Brazil needs structural reforms, and principally those that will enable the public sector to reduce its unproductive expenditures and, thus, to spend no more than it takes in. A government that spends more than it takes in competes with the private sector for resources, removing money from the economy to satisfy its own consumption needs instead of investing. The government's need for financing results in higher interest rates, which is nothing more than the price of money. And if the government decides to finance itself by printing money, it will spark inflation. Thus, the reforms are inextricably linked to the reestablishment of favorable investment and employment conditions in Brazil.

Although not yet comparable to world levels, the decline in interest rates speaks for itself.



Consumption

The notable increase in consumption after the implementation of the *Real Plan* resulted from the combined influence of growth, income

redistribution and the resumption of credit availability. This consumption increase is the most expressive indication of the change that has taken place in the post-Real period.

The immediate effect of the *Real* Plan was a strong increase in demand. Initially, it was for basic necessities like food, hygiene products and cleaning materials; and soon thereafter for goods of a higher value, such as appliances and automobiles. In the first phase, what stood out was the significant growth in the purchase of various consumer goods, such as eggs, milk, chicken and meat. However, one cannot ignore that there was a notable diversification of consumption as Brazilians bought more processed foods – like yogurt, canned goods, and various frozen foods – that were formerly inaccessible to the majority of the population.

In July 1994, one minimum salary could purchase approximately 12 bags of cement; today, it can purchase 22

CONSUMPTION OF PROCESSED FOODS
% INCREASE 1994-96

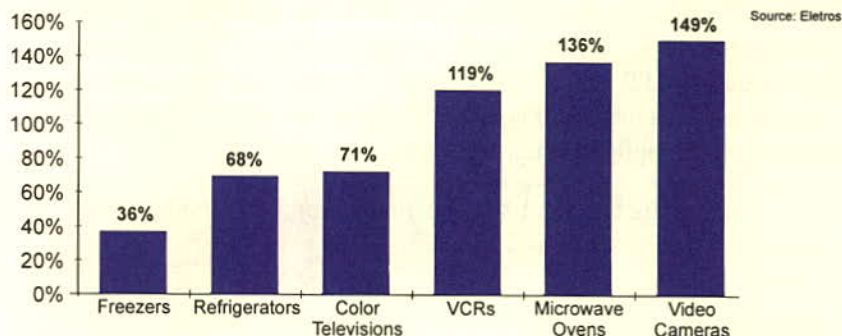
	Consumption
Processed foods	18.3
Chicken	27.8
Beef	19.4
Pork	31.1
Fish	12.3
Yogurt	87.2
Cheese	51.4
Beer	55.5
Soft drinks	58.9

Source: ABIA

Brazilians were able to consume more than food products. Included in this expanded list of consumer goods are the principal electric appliances, like refrigerators, freezers and color televisions. Addition-

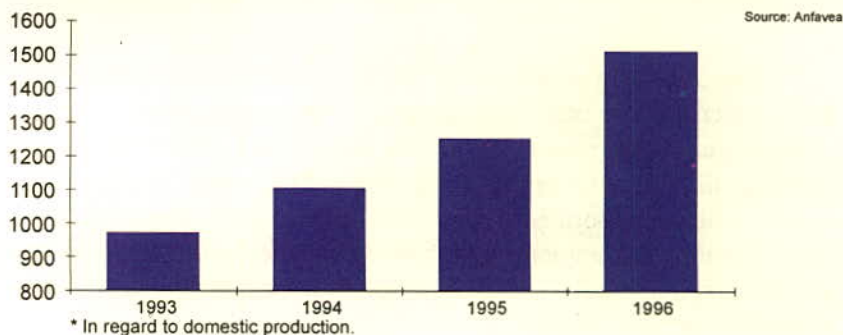
ally, a very strong demand developed for more sophisticated products like microwave ovens, VCRs and video cameras.

Sales of Electric Appliances % Increase 1994 - 1996



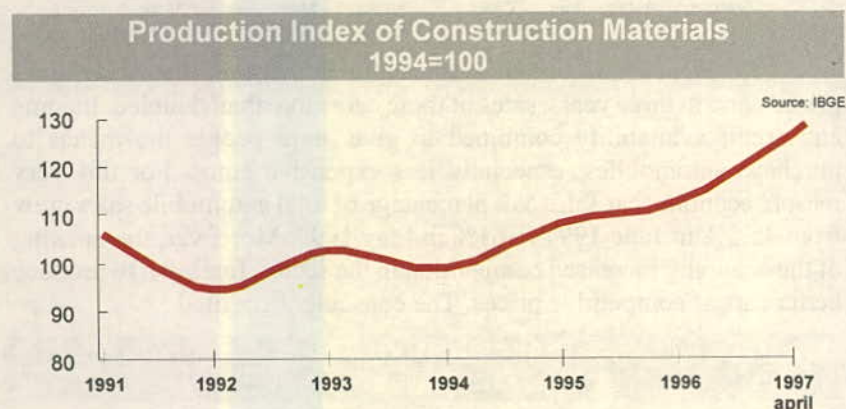
The *Real Plan* sparked a substantial increase in the sale of low-priced cars. In three years, sales of these cars more than doubled. Income and credit availability combined to give more people the means to purchase automobiles, especially less expensive autos. For this very reason, economy car sales as a percentage of total automobile sales grew from 45.5% in June 1994 to 61% in May 1997. Moreover, the opening of the economy increased competition in the sector, forcing it to produce better cars at competitive prices. The consumer benefited.

Domestic Auto Sales* (in 1,000 units)



Gradually, the *Real* Plan is making room for new products in the Brazilian population's consumption basket. Home construction materials are another important example. In July 1994, one could purchase approximately 12 bags of cement with a minimum salary; today, one can purchase 22 bags with one minimum wage. As a result, the increase in consumption was significant. Sales of portland cement in 1996 were 38% greater than in 1994. Of all the concrete produced last year, almost 80% was marketed as resales of construction material, and 53% was resold to individuals for building their own homes.

The production and sale of inputs for civil construction rose notably.



The federal government is taking other steps also to spur the development of the construction sector. The recent proposal sent to Congress to create new rules for the Real Estate Financing System (Sistema de Financiamento Imobiliário – SFI) seeks to reduce the country's housing shortage and to expand employment. The government hopes that the bill's implementation will stimulate the flow of long-term private capital into the sector, and especially from institutional investors such as the pension funds.

Investments

Investment levels have also increased as a percentage of GDP. This was the result of the improved ability to foresee developments because of stabilization, of the emergence of an enormous consumer market, and of the government's tireless efforts to reduce the Brazil Cost. Investment as a percent of GDP rose from 14% in the pre-Real period to nearly 16% in the first half of 1997. But this level is still insufficient for Brazil's needs. That is why it is necessary, through fiscal adjustment, for the government to become a net saver and for the country to create new jobs by investing more.

Annual foreign direct investment jumped from US\$1.3 billion during 1991-94, to no less than US\$9.9 billion in 1996. It will probably reach US\$15 billion in 1997

Regarding foreign direct investment, much has changed since the implementation of the *Real* Plan. The flow of these investments into Brazil has expanded significantly. While the average net inflow was US\$1.3 billion between 1991 and 1994, it reached US\$4.3 billion in 1995, US\$9.9 billion in 1996, and the forecast is US\$15.0 billion for 1997. By May 1997, US\$6.3 billion had entered the country, surpassing by 69.3% the inflows for the same period in 1996.

This change was due to the fact that investors have a more positive perception of the Brazilian economy. Decisive in this was:

- price stabilization and the renewed ability to plan;
- the macroeconomic adjustment;
- the continuing process of trade and financial liberalization;
- the National Privatization Program;
- the liberalization of laws, for instance the reduction of tax rates and the authorization of investments in formerly restricted areas; and
- the presence of an enormous and expanding consumer market.

There was also a diversification of the sectors receiving these investments. Manufacturing, which accounted for 72.3% of total invest-

ments in Brazil as of June 1995, attracted around 24% of the flows in 1996. Meanwhile, the service sector, which had previously accounted for 22.0% of total flows, captured 62% of the new inflows in 1996.

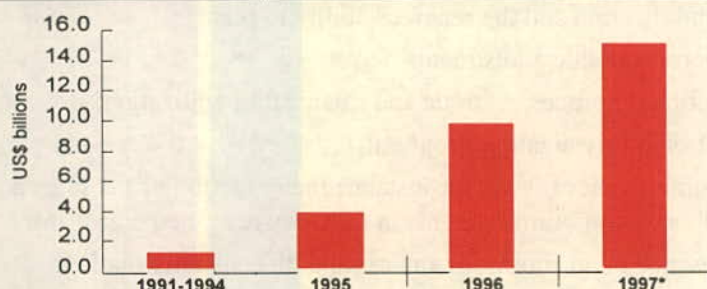
The country source of investment in Brazil changed also, with Spain, Portugal, Chile, the Netherlands and South Korea, among others, increasing their relative investment shares.

The number of companies receiving annual investments of less than US\$10 million grew continuously, increasing from 1,660 to 2,370 between 1994 and 1996. This trend indicates a more dispersed presence of foreign investors, with the average individual investment rising from US\$516,000 to US\$808,000 during the period.

Foreign direct investments bring a number of benefits to Brazil, among them:

- the introduction and dissemination of technological advancements;
- an intensification of external competitiveness and, as a result, of exports;
- an increase in employment; and
- the financing of current account deficits, through capital that tends to stay in the country for long periods.

Annual Net Inflow of Foreign
Direct Investments Into Brazil /1



1/ Includes domestic currency, commodities, conversions and reinvestment operations.

* estimate

Source: Central Bank

With a view to promoting new investments, the government has undertaken measures in specific sectors, for instance, the proposal to create the Real Estate Financing System, the Automotive Regime ("Regimes Automotivos"), and the "Brazil in Action" Program ("Brasil em Ação"), among others.

Automotive Regime

Many investments, over varying time periods, are anticipated under the General Automotive Regime (Regime Geral Automotivo). New investment resources planned for the sector during 1996-99 total R\$19 billion, distributed among 141 projects. The vehicle assembly sector plans to invest a majority of these resources, i.e., R\$14.8 billion, in 14 projects. The farm machinery sector will invest R\$0.6 billion in 15 projects. Finally, the autoparts sector will put R\$3.6 billion into 112 new projects.

Anticipated
investments
for 1996-99
will reach
R\$ 21.8 billion,
distributed
throughout
Brazil

Under the Special Automotive Regime for the Northeast/North/Central-West (Regime Automotivo Especial do Nordeste/Norte/Centro-Oeste), the combined anticipated investments of 25 companies total R\$2.8 billion.

Brazil in Action

The "Brazil in Action" Program has been created in order to assure the implementation of a new development model that is compatible with the increasing opportunities afforded by economic stabilization. This program comprises a group of 42 investment projects aimed exclusively at infrastructure and social development. It will invest R\$54.3 billion between 1997 and 1998.

The Brazil in Action Program comprises a group of projects with the dual purpose of making Brazil competitive in the world economy and of overcoming social inequalities

The projects were selected because of their ability to generate many other investments that will maintain the dynamic of economic growth in the coming decades. At the same time, these projects share a close complementary and synergistic relationship for balanced regional development. They have the dual purpose of making Brazil competitive in the world economy and of overcoming social inequalities.

An examination of the infrastructure projects reveals a consistent series of investments in transportation, energy and communications. These projects were chosen for their impact in reducing the Brazil Cost, their capacity to promote private investment, and their contribution to equalizing opportunities among regions competing for productive capital. In deciding where to invest these resources, the government took into consideration what used to be called the Axes of National Integration and Development ("Eixos de Integração e Desenvolvimento Nacional"). These six axes represent a way of rearranging the country with a view toward integrating the sparsely occupied or depressed regions into the areas that are more dynamic, as well as assuring them a link with international markets.

In the transportation sector, the Brazil in Action program has four main thrusts: the inter-modal model, the decentralization of the federal railway network, continental integration and the privatization of port operations. Investments are foreseen on nearly 7,200 km of waterways, of which: 2,250 km on the Araguaia/Tocantins/Rio das Mortes complex; 1,056 km on the Madeira river; 1,371 km on the São Francisco river; and 2,400 km on the Tietê/Paraná/Paranaíba complex. In addition to these projects, the program plans to update the capacity of another 1,000 km of the main axis of integration with Mercosul, located along the South-eastern and Southern regions, and to restore 13,000 km of highways in order to incorporate them into the interstate network. The investments

in the ports of Pecém, Suape, Sepetiba and Santos will fill the gaps in the Brazilian port system and, thereby, consolidate the transportation system that the country needs to position all of its regions more advantageously within the international market.

National Integration and Development Axes



The communications sector was included in the program with substantial investments planned to expand and to modernize telecommunications and postal services. Public and private companies will undertake these projects within the new institutional model of service concessions, which anticipates the privatization of the system by the end of 1998.

The most important step in this direction, besides the new Telecommunications Law (“Lei Geral das Telecomunicações”), was already taken in the first half of 1997: the initiation of the process granting concessions for the exploitation of Band B of the Mobile Cellular Services. However, these institutional reforms have not prevented the Telebrás System from pouring massive investments into the expansion and improvement of its fixed and mobile telephone services. In 1996 alone, three million new conventional and cellular phones were installed.

This number will be increased further this year with the installation of 5.2 million new telephones.

In the energy sector, Brazil in Action has focused on projects that facilitate the modernization of Brazil's energy profile. The projects invest in the energy transmission system which will, initially, remain under government control to facilitate the regulatory function that will be essential after the privatization of the energy sector. They are also projects that progressively change the current energy matrix, introducing the use of natural gas for power generation.

Of the transmission systems being expanded, the most notable are: the system associated with the Xingó hydroelectric plant supplying the Northeast region; the Tucuruí transmission line supplying the western region of Pará-Altamira, Itaituba and Santarém; and the interconnection of the North/Northeast and South/Southeast/Central-West systems.

Brazil in Action's principal undertakings in the natural gas sector are the Bolivia-Brazil Gasline and the transportation project for the Urucu Natural Gas in the Amazon region. The Bolivia-Brazil Gasline will begin supplying natural gas by December 1998. Thus, both Bolivian and domestic natural gas will be available to the Southeastern, Southern and Central-West regions, supplying them with clean and highly efficient energy.

Guided by the principles of decentralization, private participation and cooperation among the federal, state and municipal governments, the objective of the sanitation, housing and health projects is to combine universal access with improvement in the quality of services. The federal government's goal for 1998 is to make water supply services available to 100% of the urban population and sewage services to at least 80%. The housing programs focus mainly on assisting families with up to five minimum salaries. These groups would otherwise have no chance of being served under the new market rules that will go into

effect with the Real Estate Financing System. The measures in the health area were subdivided into two efforts. The first is directed at restoring existing facilities and strengthening the management capacity of the Unified Health Service ("Sistema Único de Saúde" – SUS). It also seeks to expand the pioneer assistance model, Community Health ("Saúde da Comunidade"), by contracting community health agents and by practicing family healthcare. The second, dedicated to pre-natal care, seeks to reduce infant mortality 50% by 1999.

To confront the crucial problem of unemployment, Brazil's great challenge at the end of this century, Brazil in Action has selected a group of projects with emphasis on job and income generation, as well as on professional training.

Focusing on basic instruction, the education projects seek to increase the stature and qualifications of teachers, as well as to meet the schools' needs, by radically decentralizing the resources for improving administration and learning.

Measures aimed at strengthening family farming and agrarian reform, a priority of this administration from the beginning, are also included in Brazil in Action. So far, 117,000 families have been resettled, i.e., 42% of the 280,000 that will be assisted by 1999.

Water resources, especially irrigation, were selected for their important role in agricultural production and in solving the problems of depressed regions like the semi-arid Northeast. The significant increase in water availability, and its adequate management, along with the expansion of agricultural irrigation, will assist the semi-arid regions to overcome their relative backwardness. By implementing a new irrigation model, with the participation of private investment, the goal is to increase productive investments and to improve the execution and administration of the irrigation projects. The results are already evident. While only 298,000 hectares were under irrigation by 1996, another 118,000 hectares will be added in 1997 alone.

BRAZIL IN ACTION

Resource Allocation by Area (1997–1998)	R\$ millions
Infrastructure	24,687.8
Social	29,671.9
Total	54,359.7
Total Value of the Projects by Sector (1997–1998)	R\$ millions
Transportation	4,640.8
Energy	3,429.0
Communications	16,618.0
Agriculture	10,324.9
Tourism	201.0
Housing	5,176.6
Sanitation	2,664.7
Health	2,382.8
Education	1,783.0
Employment	7,138.9
Total	54,359.7

The Regional Issue

The monetary stability resulting from the *Real* Plan brought the theme of Brazilian economic development back to the forefront. In this context, the regional issue takes on a new perspective.

The Brazilian legacy is one of profound income inequalities, contrasting social realities among the country's regions, and a heavy

concentration of economic activity in the South-Central region. This situation developed within the context of a closed, relatively isolated economy with high levels of import protection and excessive controls on foreign capital.

Investments are now flowing to new areas, spreading employment opportunities

The opening of the Brazilian economy increased its competitive requirements, stimulated the influx of foreign capital, and accentuated the need to integrate into external markets. There has been a restoration of private productive investments in Brazil, with the country rejoining, as we have seen, the club of nations receiving a growing share of the international flow of direct foreign investments.

Contrary to pessimistic forecasts that economic activity would be increasingly concentrated in Brazil's South-Central region, which would be greatly aggravated by the inclusion of Belo Horizonte and Porto Alegre, a significant part of the new investment is seeking new areas. Investments are going not only to the South-Central region, but also to such so-called periphery states as Bahia and Ceará in the Northeast and to Goiás and Mato Grosso in the Central-West.

A significant "relocation" movement is currently underway. Industrial plants in the consumer goods sector (textiles, clothing, etc.), previously installed in developed regions, are moving to less developed states like Ceará or Maranhão.

In the automotive industry (cars, motorcycles, trucks, autoparts, etc.), which accounts for a significant portion of national industrial production, there has been a vigorous inflow of new manufacturers into areas where this type of activity did not exist previously, for instance, the North, Northeast and Central-West. Some 25 auto sector companies are expected to invest a total of R\$2.8 billion in these regions.

**ANTICIPATED INVESTMENTS* IN THE BRAZILIAN
AUTOMOTIVE SECTOR - 1997**

Region/State	Amount (US\$ millions)
North	
Acre	13.5
Tocantins	31.8
Central-West	
Goiás	464.4
Brasília	22.5
Northeast	
Ceará	166.0
Piauí	38.0
Paraíba	339.7
Pernambuco	27.5
Bahia	1,450.2
Northeast (state undetermined)	200.0
South and Southeast	19,022.9
Total	21,776.5

(*) These investments have already been approved by the Ministry of Industry, Commerce and Tourism, or authorized for inclusion in the automotive regime defined by Law 9,440/97(North, Northeast and Central-West regions).

Source: Ministry of Industry, Commerce and Tourism

New frontiers are being established in farming, agro-industrial and mining activities. Examples are the increased grain production in the Central-West and Northeast, and the irrigated fruit production in the Northeast.

The federal government anticipated some of these changes to a certain extent in its Multi-Year Plan for 1996-99, which was expanded later in the Brazil in Action Program. It reintroduced into its planning an expressed concern about the regional impact of development, adopting the concept of national development and integration axes. The government's approval of a group of large investment projects, with an emphasis on infrastructure, contributed to restoring confidence in the Brazilian economy and to guiding the increasing flow of private investments.

Employment and Salaries

The government has been searching tirelessly for solutions to the new challenges of globalization, especially that of employment. There are four basic aspects of government policy in this area:

- a) incentives for sectors with great job creating potential;
- b) job and income generating programs through incentives to micro and small enterprises;
- c) training and qualification programs for workers; and
- d) strengthened collective bargaining procedures between workers and employers.

In 1996, the Brazil in Action Program was responsible for training more than 1.1 million workers in job qualifying and requalifying courses. By the end of 1998, the program will assist nearly 4.3 million people. Moreover, in 1996 nearly R\$5.5 billion were applied to small productive investments that create jobs. Such investments are anticipated to reach some R\$6 billion in 1997. As a result of this effort and its affect on income, it is estimated that in 1996 more than 500,000 direct or indirect jobs were maintained or created.

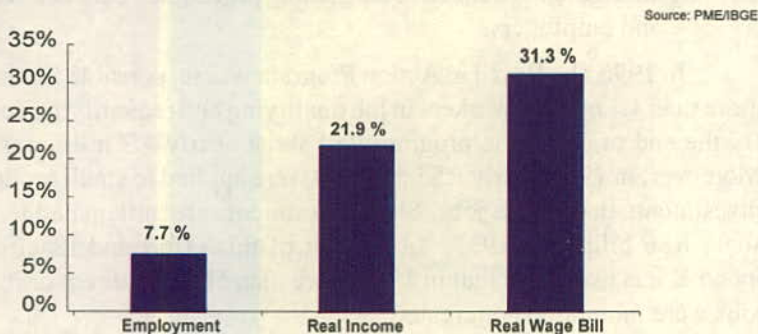
The number anticipated for 1997 is even larger: 800,000 jobs. Other measures are being implemented successfully in this area, such as the Program to Combat Slave, Child and Other Degrading Labor ("Programa de Combate ao Trabalho Escravo, Infantil e Outras Formas Degradantes de Trabalho") and the Program to Improve Work Conditions and Environment ("Programa de Melhoria das Condições e dos

Ambientes de Trabalho”). The combined effort of different ministries to fight degrading child labor met with significant success in a short time: 30,000 children were removed from work in the charcoal kilns and sugar fields and returned to school thanks to the Brazil Child-Citizen Program (“Programa Brasil Criança-Cidadã”).

Moreover, measures were adopted to de-index salaries gradually, providing a significant increase in negotiating room between workers and employers. In addition, one should highlight the Provisional Measure (“Medida Provisória”) that made it possible for the workers to participate in profit-sharing, an innovation that strengthens and facilitates salary negotiations.

Since the beginning of the *Real* Plan, according to information from the IBGE’s Monthly Employment Survey (“Pesquisa Mensal de Emprego” – PME), some 1,151,000 new jobs were created in just six of Brazil’s principal metropolitan areas.

Employment, Real Income and Real Wage Bill
for the third year of the *Real Plan* in relation to the year immediately prior to the Plan % Growth



The unemployment rate remained low in the third year of the *Real* Plan, at a level almost equal to that of the year immediately prior to the Plan’s implementation. The unemployment rate in Brazil is relatively low compared to that of other industrialized countries and to that of the Latin American economies.

**BRAZIL
TREND OF OPEN UNEMPLOYMENT RATE**

Year	Rate (%)
1992	5.76
1993	5.31
1994	5.06
1995	4.64
1996	5.42

Source: IBGE

**URBAN UNEMPLOYMENT RATE – 1996
FOR SPECIFIED COUNTRIES**

Country	Rate (%)
Germany	10.4
Argentina	17.2
Chile	7.2
Spain	22.7
United States	5.4
France	12.4
Italy	12.1

Source: IMF and ECLAC

Moreover, both the average income and the total earnings of workers increased, in real terms, significantly more than did GDP during the *Real Plan*: 21.9% and 31.3%, respectively. The results show how much salaries have grown as a percentage of Brazil's national income.

Salaries are growing as a percentage of national income

The minimum salary has not been forgotten. Unlike in the past, when unrealistic increases were unsustainable due to an inflation process that rapidly depreciated them, the minimum salary has been steadily recovering. Having been set in May 1997 at R\$120.00, the minimum wage is 21.3% more, in real terms, than it was in July 1994.

THE ANNUAL AVERAGE MINIMUM WAGE – 1980-96

Year	Average minimum wage (US\$)*
1980	75.32
1981	86.92
1982	89.98
1983	62.71
1984	51.52
1985	50.58
1986	56.30
1987	52.77
1988	58.20
1989	75.56
1990	75.44
1991	75.93
1992	64.92
1993	74.93
1994	74.30
1995	99.19
1996	107.41

Source: Central Bank; Preparation: IPEA/DIPES

(*) Converted by the average monthly rate

III. THE AGRICULTURAL SECTOR

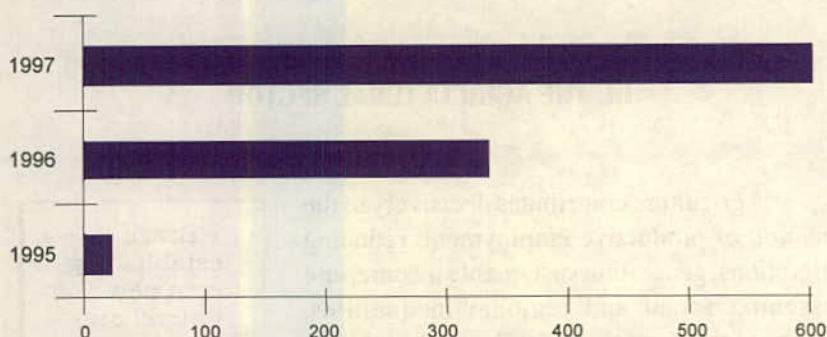
Agriculture contributes decisively to the creation of productive employment, reducing migrations, generating sustainable income, and lessening social and regional inequalities. Aware of this fact, the federal government has adopted various measures to stimulate the sector, strengthening family farming, refining financial and commercial instruments, improving the infrastructure conditions, providing scientific and technological support, and assisting the sector's entry into the international market. The following are some of the principal measures taken in the last three years and their results.

Brazil is
establishing
a new
level of
production

National Program to Strengthen Family Farming (Programa Nacional de Fortalecimento da Agricultura Familiar - Pronaf)

The National Program to Strengthen Family Farming seeks to assist family farming and to stem the rural exodus by decreasing rural poverty, by creating productive employment and by improving rural income. In 1995, PRONAF expenditures were R\$36 million, benefiting 19,000 families; in 1996, R\$650 million were spent, benefiting 333,000 families, a significant increase. For 1997, expenditures should reach R\$1.5 billion, benefiting 600,000 families. The cost of the Program's loans has fallen significantly, from 11.7% to 2.0%.

National Program to Strengthen Family Farming (PRONAF) Families Benefited (thousands)



Improving the Financial and Commercial Instruments

One aspect that stands out in this area is the securitization of rural debt, benefiting nearly 350,000 farmers, the vast majority of whom have small- and medium-sized operations. This measure, involving resources on the order of R\$7 billion, was essential to end the crisis affecting this sector.

With regard to financing, the federal government adopted several measures seeking to increase the flows of resources into agribusiness activities. The "63 caipira," created to expand external financing, attracted US\$5.3 billion for the sector in 1996. The government sought also to increase financing with domestic resources by raising from 17% to 25% the percentage of their deposits that banks must lend to the sector. Moreover, the credit operations involving Rural Producer Notes and Rural Promissory Notes ("Notas do Produtor Rural" and "Duplicata Rural") had their rates reduced to zero. In the case of PROAGRO, the tax on financial operations (IOF) was reduced by 57%, on average.

In the tax area, the sales tax (ICMS) on exports was eliminated, representing a potential income gain of 13% for basic products and 6% for semi-finished goods. Recently, the PIS/COFINS refund was expanded, representing a cost reduction of up to 5.3% for agro-industrial exporters.

New instruments were created also to facilitate the commercialization of agricultural products, and notably the contract options for corn, rice, cotton and wheat. These instruments function like a price guarantee, through payment of a premium, while avoiding the need to sell the products to the government.

The Harvest Plan

Each harvest year the federal government, through the Ministry of Agriculture, further improves its support instruments for the Brazilian producer. The 1997-98 Harvest Plan, for example, contains some important modifications.

First of all, the government issued an early announcement of its new regulations, making it possible for farmers to formulate and implement their plans.

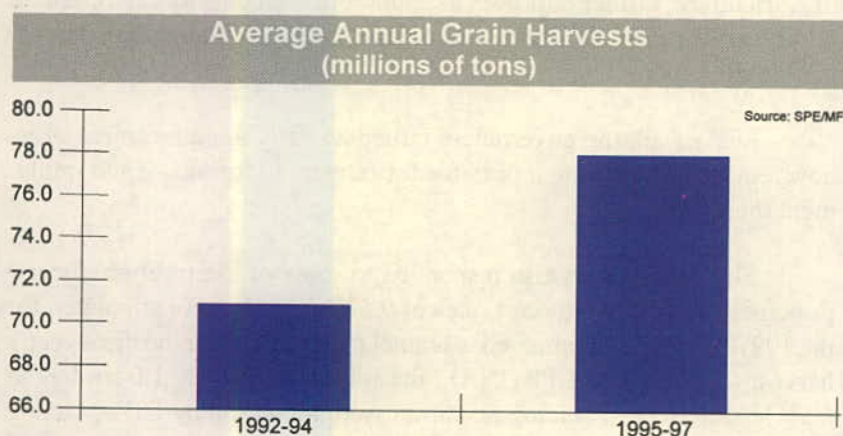
The government also responded to some of the rural producers' principal complaints. Interest rates of 9.5% per year were stipulated for the 1997-98 harvest, compared to annual rates of 12% for the prior year's harvest (in the case of PRONAF, the rates were reduced from 9% to 6.5%). Moreover, financing resources were increased by 60%, totaling R\$8.5 billion (in the case of PRONAF, the available resources increased by more than 100%, reaching the level of R\$1.65 billion).

Infrastructure Improvements

Regarding infrastructure improvements, it is worth mentioning the efficiency gains achieved through the privatization of the railroads, as well as the expansion of new river shipping routes through the Madeira, Tocantins-Araguaia, Paraguai-Paraná and São Francisco waterways, creating opportunities for new investments. We are dealing with a change in the logistics of transportation, promoting the restructuring of economic activities throughout the entire country and establishing the Central-West region as a new center of agricultural production.

Results

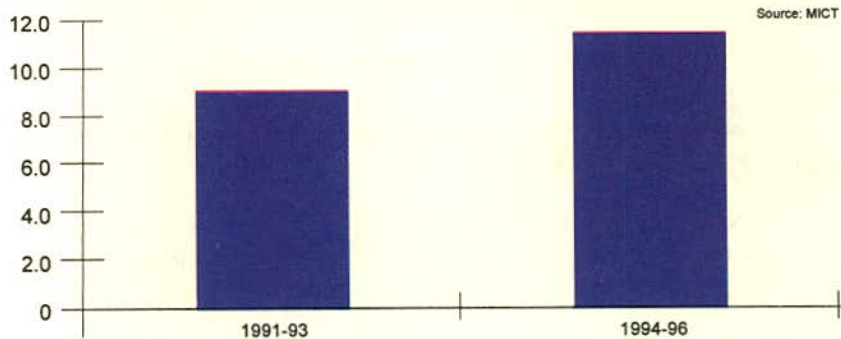
The average annual grain production in the first three years of the *Real* Plan reached nearly 78 million tons, which represents an increase of 10% over the average during the three years prior to the *Real*'s implementation. Thus, despite the poor harvest in 1996, an annual production level of approximately 80 million tons has been established.



Increased rural production was fundamental in maintaining domestic supply, contributing to the price stability of the basket of basic food items. Moreover, the agricultural sector was able to produce a surplus for export. In the first three years of the *Real* Plan the annual export value was, on average, US\$11 billion compared with US\$9 billion during the 1991-93 period – an increase of some 22%.

The data below, in addition to demonstrating the productive capacity of Brazil's farmers, confirm the appropriateness of government policies.

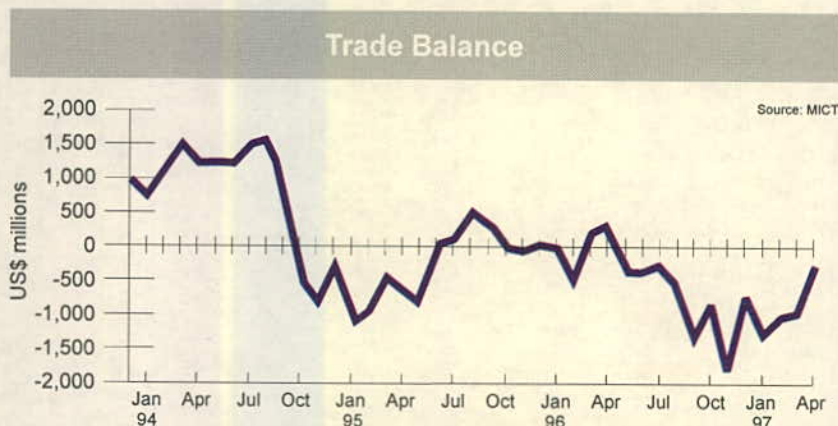
**Average Annual Exports of Basic Products
(US\$ billions)**



IV. THE FOREIGN TRADE BALANCE

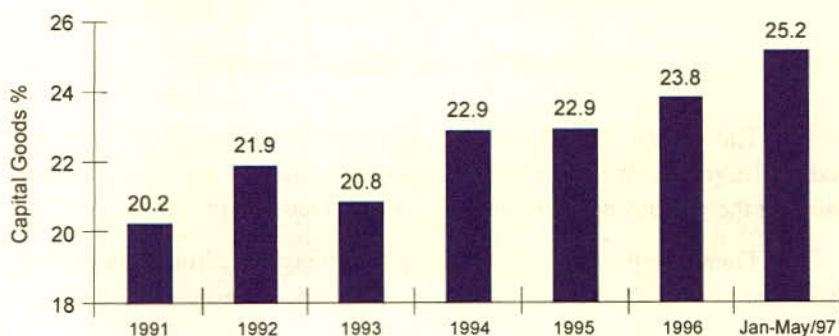
The trade balance has been registering a gradual reduction in the monthly deficit.

Export receipts have increased consistently, less in some sectors and more in others like soybeans and footwear that have benefited from the government's adoption of credit, taxation and other incentive measures.



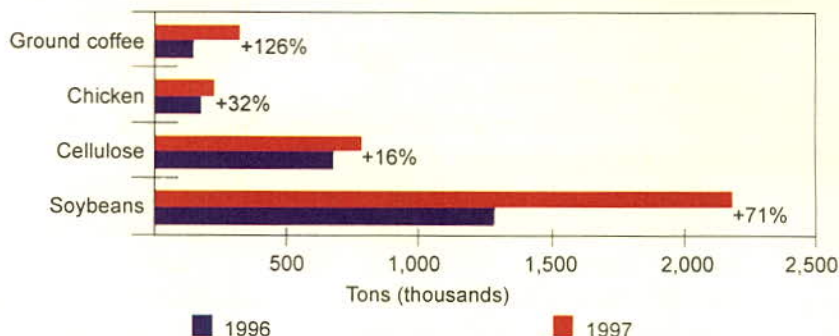
For its part, the growth in imports reflects to a large degree the increased purchase of capital goods that are important for both restoring Brazil's national competitiveness and for renewing its industrial park. As can be seen in the following graph, capital goods have represented a growing share of total imports since implementation of the *Real Plan*. This trend is the result of the productive investments that are being made in the country due to price stability and the prospects for economic growth. Incorporating the latest technology available in the international market, the imported machinery and equipment allow Brazil to restore and to expand its productive capacity.

Capital Goods Purchases as a Percentage of Total Imports



There has been a strong quantitative increase in the export of ground coffee, chicken, cellulose and soybeans in large part because of government policies. In addition to this increased volume of sales, export receipts are benefiting also from higher international commodity prices, particularly for coffee and soybeans.

Exports Jan-Apr 1997/96



V. REDUCING THE "BRAZIL COST"

The Brazil Cost is truly a major obstacle to the growth and competitiveness of the Brazilian economy. There is a collective effort among the various government agencies to face this problem.

There are three principal groups of measures already underway: stimulating exports, reducing infrastructure costs, and lowering investment costs.

Stimulating Exports

The following specific, direct measures taken to stimulate exports are worth mentioning:

1. Tax relief. Primary and semi-finished goods represent no less than 40% of Brazil's exports. The ICMS tax on these exports has been eliminated. The government has also eliminated the PIS/PASEP and COFINS taxes on materials used in the production of goods for export or for sale in the domestic market to exporting companies.
2. Regulation of export credit insurance. This measure seeks to protect Brazilian exports of goods and services against commercial, political and extraordinary risks that affect economic and financial transactions linked to export credit operations. In the event of difficulties with the importer of the Brazilian product, the exporter will be "protected" by the insurance.
3. Financing exports and reducing related capital costs. Among these measures are: a) an extensive reformulation of the Export Financing Program ("Programa de Financiamento às Exportações" – PROEX), expanding the list of eligible products and extending financing to the production phase to make it more

attractive and effective. Whereas the government paid out US\$82 million and US\$115 million in 1995 and 1996, respectively, expenditures of no less than US\$1 billion are anticipated for 1997; b) the widespread restructuring of the National Bank for Economic and Social Development (Banco Nacional de Desenvolvimento Econômico e Social – BNDES) to make it a key element in the financing of Brazilian exports. To this end, an export financing line of R\$1 billion was created at the Bank for use by sectors like footwear, autoparts, clothing, and furniture. In addition, the financing term for capital goods exports was increased to 10 years, through Finamex, an export financing line of the BNDES; c) the setting of a zero IOF tax rate on external resources aimed at financing export companies.

4. Other measures, like the creation of the so-called “dry ports” which, by decentralizing customs procedures to the regions in which the goods are produced, decongest the ports and airports, saving time and money.

Reducing Infrastructure Costs

It is estimated that just the leasing of the Santos port to the private sector will reduce the cost of loading a container from the current R\$500 to R\$150.

The most general measures to reduce infrastructure costs tend to have a positive impact on every sector of the economy, including naturally the export sector. These measures include the following initiatives:

1. Modernizing management of the stevedores.
2. Simplifying the structure of port duties (it has already been possible to reduce from 18 to 7 the number of different duties charged).

It is estimated that just the leasing of the Santos port to the private sector will reduce the cost of loading a container from the current R\$500 to R\$150

3. Making more flexible the concession, leasing and privatization processes and, especially, breaking up the state monopolies in the fundamental infrastructure areas needing investment, such as railroads, ports, telecommunications, energy, highways and waterways. On this point, it is worth mentioning the benefits that are already visible. The private sector concession of cellular phone services will reduce consumer costs impressively. In the Federal District alone, where the winner of the bidding process has

already been decided, the cost of a phone will fall from R\$330.00 to R\$158.40, a reduction of 52%. The cost for calls will decline, on average, by 30%. Businesses will benefit immediately from the significant decrease in port service costs. In addition, with the soon-to-be-concluded privatization of the railroads, a significant jump in investments in the sector is anticipated, reaching an estimated R\$4 billion. The companies that purchased the railroads have committed themselves to guaranteeing that the number of accidents will be reduced by at least 40% by the fifth year of operation. Finally, the investment in the Madeira Waterway (in the Amazon region) is expected to reduce the cost of transporting grains to Rotterdam, for example, from R\$105/ton to R\$70/ton.

Lowering Investment Costs

The third group of measures designed to reduce the Brazil Cost is comprised of direct efforts to reduce the cost of investments. Among them, the following deserve mentioning:

1. Reducing to zero the import tax rate for capital goods, computer technology and telecommunications equipment. Capital goods, both domestic and imported, will also be exempted from the IPI;
2. Reducing and simplifying, through the Integrated System for the Payment of Taxes and Contributions of Micro-Enterprises

and Small Size Business ("Sistema Integrado de Pagamento de Impostos e Contribuições das Microempresas e das Empresas de Pequeno Porte" – SIMPLES), the taxes and contributions paid by small- and medium-sized companies;

3. Reducing the rates of the Income Tax on Legal Entities ("Imposto de Renda sobre Pessoa Jurídica" – IRPJ) from 25% to 15% and of the Social Tax on Net Profit ("Contribuição Social sobre Lucro Líquido" – CSLL) from 10% to 8% for business in general and from 23% to 18% for financial institutions and insurance companies;
4. Recalculating the TJLP (long-term interest rate based on BNDES loan rates) in order to reduce it;
5. Allowing the borrowing of external resources to finance both farm production and activities of industries linked to the sector, as well as reducing the interest rate for the 1996-97 agricultural harvest.

Until recently, no serious effort had been made to reduce the Brazil Cost. Today, three years after the implementation of the *Real* Plan, it is true that we still have plenty to accomplish. However, it is also true that we have achieved a number of successes.

VI. PUBLIC SECTOR ACCOUNTS

Of all the challenges to the sustainability of the *Real Plan*, the public deficit is undoubtedly the one that requires the most attention. It is through a true fiscal adjustment, at the state and municipal levels as well as at the federal level, that the basis can be established for sustained economic and social development over the medium and longer term without inflationary pressures.

The results of all the measures related to the behavior of interest rates are beginning to appear in the main fiscal statistics, and they are positive

Given the pressing need to reorganize the public accounts in order to stimulate savings and, thereby, to create the conditions for investing and generating employment, the government has been making a persistent effort to achieve fiscal equilibrium.

A few measures were implemented even before July 1994. Among them was the creation of the Social Emergency Fund ("Fundo Social de Emergência" – FSE), which later became known as the Fiscal Stabilization Fund ("Fundo de Estabilização Fiscal" – FEF). The objective of the FEF is to break, temporarily, the relationship between receipts and their distribution until the approval of the constitutional reforms enables the federal government to allocate public resources more efficiently.

The federal government did more, however, than create and extend the FEF and press for the approval of the constitutional reforms. In addition to these steps, it also struggled to facilitate the privatization programs at both the federal and state levels.

Federal government measures to end the public deficit

At the federal level:

- Reformulated the guidelines for the budget/financial program, harmonizing the budgetary process with its financial implementation.
- Developed an expenditures calendar for all the public bodies utilizing budget resources.
- Programmed expenditures according to the project and sector of activity.
- Tightened the control on personnel expenditures through a series of discreet actions, e.g., by improving the management of wage and salary payments.
- Improved the tax system by changing several tax laws, such as the corporate income tax.
- Created the *Brazil in Action Program*. This program, seeking to improve the allocation of budget resources, stresses investments that give priority to economic and social development.
- Undertook several actions in the Social Security area that are designed to increase receipts and to control expenditures. Of special relevance were the changes made in the rules for granting special retirements.

At the state and municipal levels:

- Allowed the Federal Savings Bank ("Caixa Econômica Federal") to help solving the financial problems of states that are willing to reform their fiscal situation.
- Adopted mechanisms to help the state financial institutions, looking toward their privatization or transformation into development agencies.
- Refinanced state government debts through the Program to Assist the Restructuring and Fiscal Adjustment of the States ("Programa de Apoio à Reestruturação e ao Ajuste Fiscal dos Estados"). These programs encourage the collection of taxes and discipline expendi-

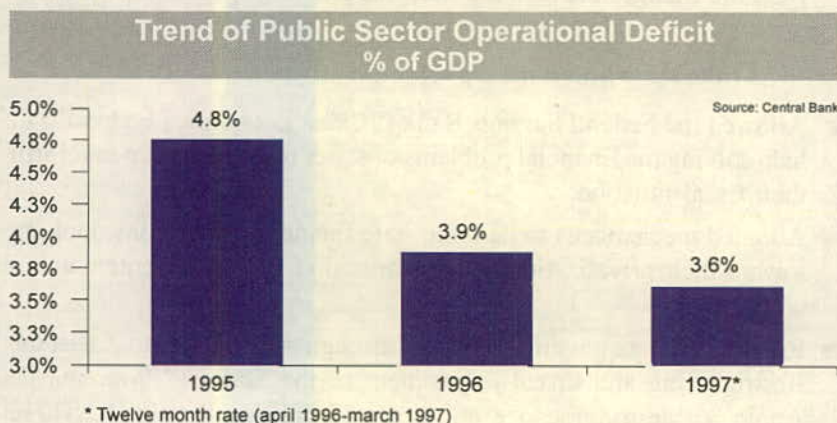
tures. They promote also the gradual reduction of state debts through the sale of state companies and the granting of public service concessions.

At the level of federal government enterprises:

- Strove to control current expenditures.
- Managed wage negotiations firmly.
- Prohibited measures seeking to increase the transfer of resources from the enterprises to closed retirement systems.
- Identified assets not being utilized for operations so that they could be employed to reduce debts or could be used for investments to improve operations.

Results

The results of all these measures, combined with the behavior of interest rates on public debt instruments, are beginning to appear in the principal statistics on fiscal affairs. According to the Central Bank, the operational deficit of the public sector has been gradually declining since it reached 4.8% of GDP in 1995. During 1996, it fell to about 3.9% of GDP; as of March 1997, it approximated 3.6%.



VII. THE PRIVATIZATION PROGRAM

The National Privatization Program ("Programa Nacional de Desestatização" – PND), established in 1991 to help modernize the Brazilian government, gained renewed strength with the *Real* Plan. As shown in the following table, of all the revenues received during the Program's seven years of existence, close to 53% were collected after July 1994, namely, in three years.

NATIONAL PRIVATIZATION PROGRAM – 1991-1997

US\$ millions ¹

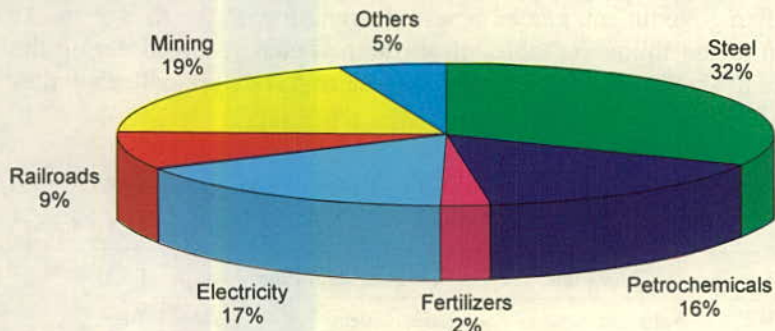
Before the <i>Real</i> Plan				Since the <i>Real</i> Plan			Total		
	Sales receipts	Debt transferred	Total	Sales receipts	Debt transferred	Total	Sales receipts	Debt transferred	Total
Productive Sectors	8,147	3,480	11,627	4,566	4,517	9,082	12,713	7,996	20,709
Steel	4,858	2,626	7,485	703		703	5,561	2,626	8,188
Petrochemicals	2,135	773	2,908	564	230	793	2,698	1,003	3,701
Fertilizers	418	75	494				418	75	494
Mining				3,299	4,287	7,586	3,299	4,287	7,586
Others	736	5	741				736	5	741
Infrastructure and public services				4,565	851	4,955	4,565	851	5,416
Railroads				1,477		1,477	1,477	—	1,477
Electric				2,890	588	3,478	2,890	588	3,478
Others				198	263		198	263	461
Total	8,147	3,480	11,627	9,131	5,368	14,037	17,278	8,848	26,125

(1) Takes into consideration the effective date of the sales of the shares.

Source: BNDES

The sale of CVRD (the Vale do Rio Doce Company) virtually ends the privatization of industrial firms and initiates a new phase that focuses principally on privatizing infrastructure assets and on granting public service concessions.

**Federal Government Privatizations - 1991 - 1997
by sector**



The first phase of the PND stressed basically the privatization of steel, petrochemical, fertilizer and mining companies. A total of 46 firms were shifted to the private sector, of which 20 were sold after July 1994.

The steel sector is an excellent example of the program's success. After being privatized, the sector increased its production and its productivity to the point that it came to account for a larger percentage of Brazil's exports.

The privatizations are already beginning to show concrete results: an increase in investments and a decline in prices

In its second phase, the PND focuses on transferring infrastructure operations to private owners and on granting public service concessions. This phase began with the sale of the electric distribution firm ESCELSA in July 1995, followed in 1996 by concessions for the five principal networks of the Federal Railway (RFFSA) and for the electric distribution company of Rio de Janeiro (LIGHT). This phase will

allow private investments in sectors that are crucial to the country's economic development.

The changes taking place in Brazil's transport system are a good example of the concrete results that are already visible. With the transfer of the five principal networks of the RFFSA to the private sector, investments are again occurring in the railway sector after having been stagnant for almost two decades. More than 2,100 kilometers of railroad are under construction. The investments underway in the Northern Railway (FERRONORTE) are of special note. Some R\$400 million, out of a total program of R\$2.5 billion, have already been invested in a project to extend it by 1,728 km. Taken together, the railroad investments during the next few years should surpass R\$4 billion.

At the same time, concessions are being granted to operate ports and federal highways. One can already see significant reductions in the charges for port services. It is expected that, as the process continues, these charges will decline dramatically.

In the case of the federal highways, the outstanding concessions have been those granted in 1996 for the highway between Rio de Janeiro and São Paulo and the highway between Juiz de Fora and Rio de Janeiro. The investments planned for these two stretches of highway exceed R\$1 billion. One can already note the improvements in road signals, maintenance, installation of emergency medical services, and other items.

The program of telecommunications concessions should begin effectively during 1998. Nevertheless, people can already sense the concrete benefits coming from the privatization process. For example, it has already been announced that the private sector will reduce the cost of cellular telephone services.

VIII. SOCIAL EXPENDITURES

The federal government's expenditures in the social area during 1996 were, in real terms, 26.7% larger than in 1994. This growth was significantly greater than the rate of population expansion (2.7%) during this period. As a result, the per capita outlay of the Brazilian federal government rose from R\$491 in 1994 to R\$605.80 in 1996.

Federal expenditures on programs for the aged, the handicapped and the unemployed (social security, unemployment compensation, professional training and agrarian organization) grew the most during the years 1994-1996: 43.7% in real terms. Social outlays designed to improve the living conditions of the lowest income sectors of the population (health programs, basic sanitation, social support) increased 14.6% during the same period.

The rise in the federal government's social expenditures between 1994 and 1996 occurred at the same time that responsibility for managing these social activities was being decentralized to the states and municipalities. In a number of sectors (education and culture, nutrition, health, basic sanitation, environment, social assistance, housing and municipal planning, and employment and labor protection), the financial transfers to the states and municipalities accounted for an increasing share of federal social outlays. For example, direct federal expenditures in education and culture as a percentage of total expenditures in these areas declined from 82.3% in 1994 to 76.5% in 1996. At the same time, however, federal transfers as a percentage of total expenditures in these areas rose from 4.9% to 6.5% in the case of transfers to the cities.

Federal
government
social
expenditures
per capita
increased from
R\$ 491 in 1994
to R\$ 605.80
in 1996

SOCIAL EXPENDITURES BY THE FEDERAL GOVERNMENT (1994-1996)
Thousands of constant value December 1996 R\$

Area(*)	1994	1996	96/94(%)
Old age, disability and unemployment coverage	45,949,392	66,022,219	43.7
<i>Social Security</i>	43,291,876	61,128,143	41.2
Benefits paid by INSS	30,406,262	43,271,322	42.3
Benefits paid to federal employees	12,885,614	17,856,821	38.6
<i>Unemployment insurance</i>	2,116,903	3,491,373	64.9
<i>Job training</i>	508	262,536	51,580.3
<i>Agrarian reform</i>	540,105	1,140,167	111.1
Assistance to the low income population	10,440,700	11,967,184	14.6
<i>Medical assistance</i>	8,776,666	10,082,232	14.9
<i>Basic sanitation</i>	674,216	688,610	2.1
<i>Welfare assistance</i>	989,818	1,196,342	20.9
Youth and infant assistance	1,808,092	1,882,956	4.1
<i>Basic education (**)</i>	1,070,795	1,158,288	8.2
<i>School lunches (***)</i>	664,256	465,287	-30.0
<i>Education for children to 6 years old</i>	73,041	259,381	255.1
Others	17,028,401	15,426,757	-9.4
Total expenditure (****)	75,226,585	95,299,116	26.7
Population (thousands)	153,213	157,319	2.7
Total per capita expenditure (R\$)	491.0	605.8	23.4
Total expenditure/GDP (%)	11.8	12.3	4.2

Source: DIPOS/IPEA.

(*) The concept of area of activity is used because it better indicates the real activity financed by public funds, regardless of what agency is actually spending the funds. Thus, it must be emphasized that these figures cannot be compared with traditional measurements based on the expenditures of the ministries (institutional approach), nor with measurements based on expenditures by ministry or by function/program aggregate outlays that, in general, combine different types of real expenditures.

(**) Does not include the school lunch program, the portion of the Salary-Education collected by the states and the Federal District, nor the direct investments undertaken by the federal government.

(***) The changes in the procedure of transferring resources to the states and municipalities to finance the school lunch program led to this decline in outlays. Since 1993, the funds to finance the school lunch program during the first three months of the year are transferred in December of the preceding year. In 1996, the transfer made in December covered only nineteen days in January 1997. Thus, there was a decline in the amount of resources dedicated to the lunch program compared to earlier years. In fact, however, federal outlays in 1996 were sufficient for 163 days of the program whereas they covered 156 days in 1995 and 100 days in 1994.

(****) Total federal government social expenditures as defined by DIPOS/IPEA.

The monetary stability resulting from the *Real* Plan strengthened the effectiveness of the federal government's expenditures. Resources are no longer severely depreciated by inflation during the sometimes extended period from the time an expenditure is approved and resources allocated to the time the expenditure is actually made. Ending this corrosive effect on resources strengthened the effectiveness of outlays tremendously. This effect was especially true for those outlays implemented at the local level and/or in partnership with the states and municipalities because the gestation period for such programs is normally longer.

**SHARE (%) OF FEDERAL GOVERNMENT DIRECT
AND INDIRECT SOCIAL EXPENDITURES, BY AREA**

Areas	Direct expenditures	Transfers		
		States and DF	Municipalities	Private inst.
Education and culture				
1994	82.3	12.0	4.9	0.8
1996	76.5	15.5	6.5	1.5
Food and nutrition				
1994	2.6	53.7	43.7	0.0
1996	1.9	25.0	72.5	0.6
Health				
1994	91.0	5.6	1.8	1.6
1996	83.8	3.8	10.9	1.5
Sanitation and environ. protection				
1994	73.5	10.2	15.7	0.6
1996	38.6	31.7	28.8	0.9
Social welfare				
1994	74.2	3.2	8.8	13.8
1996	66.0	31.4	2.2	0.4
Housing and urbanism				
1994	88.9	3.2	7.9	0.0
1996	82.1	7.4	10.5	0.0

Source: IPEA/DIPOS

IX. HEALTH

The *Real Plan* sparked very positive changes in the health sector. Besides enlarging and diversifying the consumption of food-stuffs, and contributing to the improvement of the population living standard, it produced a genuine increase in the government's budget for the Ministry of Health.

These resources rose close to 16% between 1993 and 1994. During the two-year period 1995-96, the average annual outlay represented a 65% increase relative to the early years of the decade. It is estimated that the federal government alone will spend some R\$19 billion on health services in 1997. Namely, outlays per capita should approximate R\$119, or almost twice the amount spent in 1993.

The delays in paying for health services were a chronic problem during the time of high inflation rates, and one that had a negative impact on hospitals and other health care providers. Not being paid until 60 days after providing a medical service meant that, during an inflationary period, the payment was worth less than when the bill was initially issued. This situation caused services to deteriorate. The economic stability caused by the Real Plan allowed bills to be brought up to date, ending the payment delays and the constant changes in the costs of medical services.

In the communities of the 2,563 cities where the Children's Pastoral Program exists, infant mortality fell from 4 per 1,000 children born alive in 1992 to 31.4 in 1994 and 17.6 in 1996

In 1994, 56% of SUS (federal health program) resources was spent on interned patients and 44% on ambulatory patients. By the first half of 1996, the percentages had been inverted: 49% for hospitalized patients and 51% for ambulatory patients.

The greater availability of financial resources permitted larger expenditures on essential services to improve the health conditions of the most vulnerable sectors of the population. This change has been especially true since 1995 when the government created and gave priority to the Program to Reduce Infant Mortality (PRMI). This program made it possible to integrate several activities related to pre-natal care, nutrition, immunization and basic sanitary practices, in addition to those activities inherent in the work of the Community Health Agents and in sanitary education programs.

Of the 913 municipalities covered by the Program to Reduce Infant Mortality, 77% are already included in the Food Supplement Program "Milk and Health" that serves three million mothers and children. Moreover, 39% of these cities were provided water, sewage and improved housing, serving 1.2 million people directly and 3.8 million indirectly. The national average for normal immunization (75%) has been substantially surpassed in the areas served by the PRMI, where 97% of children are vaccinated before they are one year old.

The Program of Family Health Teams, begun in 1994, and the Community Health Agent Program aim to change the way health services are provided to the public. This effort combines traditional medical services with a series of measures to improve living conditions. The program has become the entrance to SUS as it seeks to resolve at this level of service the largest possible number of problems.

The Community Health Agents and the Family Health Teams programs have grown rapidly during the three years of the *Real Plan*. The number of Agents grew from 29,000 in January 1995 to more than 44,000 in 1996, providing services to some 26 million people. The current 847 Teams, serving 850,000 families, will grow to 3,500 by the end of 1998, when they will be assisting 3.5 million families.

Between 1994 and 1996, the System of Information of the Community Health Agents (PACS) allowed the identification of a group of indicators for the areas where the program is working.

The following table shows the mortality rate for the areas covered by the PACS. The decline in the rate is impressive: from 82.6 deaths per 1,000 live births in 1994 to 51.5 deaths per 1,000 live births in 1996. This decline represented a 37.7% drop in the infant mortality rate during the period. It is estimated that 6,500 deaths were avoided.

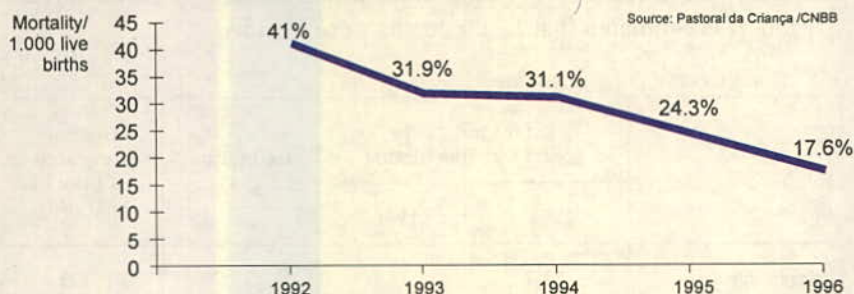
	Infant mortality (per 1,000 live births)		Reduction (%)	Deaths prevented (less than one year old)
	1994	1996		
Maranhão	71,2	48,6	37,7	491
Piauí	67,3	43,0	36,1	445
Ceará	80,0	45,7	42,9	2.967
Paraíba	90,5	53,8	40,6	637
Pernambuco	101,4	54,9	45,9	1.335
Sergipe	93,6	63,9	31,7	156
Bahia	110,9	53,0	52,2	458
Nordeste	82,6	51,5	37,7	6.489 **

(**) Data for the areas covered by the Community Health Agents program in cities that have information for all the months of the study. The states of Rio Grande do Norte and Alagoas were not included because they did not provide information in 1994. However, their data were added to the totals for all of the Northeast for 1996.

Source: PACS Information System – COSAC/SAS/MS.

It is important to remember that the PACS were placed in municipalities with a high risk of infant mortality. Priority was given to localities in those municipalities where the situation was the worst, namely, in rural zones and suburban areas.

Trend of Mortality Rate for Children less than one Year old as Registered by the Children's Pastoral Program of the National Conference of Brazilian Bishops (CNBB)



The drop in infant mortality is reflected also in the Children's Pastoral Program of the National Conference of Brazilian Bishops (CNBB). According to its data, the mortality rate fell from 41 per 1,000 live births in 1992 to 31.4 deaths in 1994, and 17.6 deaths in 1996. In this last year alone, the death of some 5,000 children was avoided in 2,563 cities. This rate cannot, however, necessarily be applied to the total population of these cities. Still, this decline in infant mortality is highly significant because the Children's Pastoral Program works exclusively with poor families.

X. EDUCATION

The third year of the *Real Plan* was marked by the implementation of actions with strong impact that are changing the currents of Brazilian education.

In 1996, the institutional changes became a reality with the passage and implementation of the constitutional amendment that creates the Fund for the Development of Basic Education and for the Improvement of Teachers (Fundo de Desenvolvimento do Ensino Fundamental e Valorização do Magistério). This action is crucial to fulfilling the priority being given to basic education.

In 1997 there will be new successes, such as the National Informatics Program in Education for restructuring professional technical training

Substantial success has been achieved in the struggle to improve the quality of instruction. The national test of students ("provão") demonstrated the real conditions of university education in our country. Similarly, the technical evaluation undertaken of textbooks financed and distributed by the government was the first one in the country's history.

Several other successes should also be noted, such as the implementation of the School by TV Program, the accelerated decentralization of the school lunch program, and others.

1996 was the year of education, when new winds blew in a strong trend toward better education in our country, giving priority to primary education among other things. In 1997 there certainly will be new advances, such as a restructuring of professional technical training, the National Program of Informatics in Education, and a constitutional amendment granting effective autonomy to the universities.

The following describes some of the principal programs, actions and achievements in the education sector.

Registrations in primary education are growing at a figure of more than one million per year

In 1994, there were 32,048,420 students registered to begin primary education. In 1996, this number jumped to 33,131,270. Of these, 88% were children in the public schools. A total of 3,982,468 students registered to study in the public sector middle schools. In 1996, this number rose 14.56%, reaching 4,562,558. During the same period, the number of students registered in the private schools increased 11.78%, going from 1,052,499 to 1,176,519.

These data suggest that primary education is gradually becoming universal in the country. There is less truancy and less repetition of grades. As their social conditions improve, families prefer to give their children more education rather than quickly sending them out to work in order to increase the family income.

At the government's initiative, a constitutional amendment created the Fund for the Development of Basic Education and for the Improvement of Teachers. It permits, beginning in 1998, the automatic allocation of R\$12 billion to primary education, which works out to R\$300 per student in all municipalities. The average per student today is less than R\$100. The fund will permit also an increase in teachers' salaries so that the national average will approximate R\$300.

Investments in education – the Fund for the Development of Basic Education and for the Improvement of Teachers provides R\$300 per student per year

Since 1995, the Program for the Maintenance and Development of Primary Education has transferred resources directly to the state and municipal schools.

Program for the Maintenance and Development of Primary Education – money in the school

In 1995, more than 100,000 schools in 200 cities received R\$228,700,000. In

1996, R\$262,800,000 was given to some 170,000 schools, benefiting more than 31 million students.

In 1997, when the NGOs involved in special education will be included, R\$272,000,000 will be sent to the schools. Those schools that participate in the Community Solidarity Program will receive 30% more than the established rates.

The Textbook
Program – more
books for
primary schools

Since 1995, all of the 33 million students in the primary grades receive their textbooks at the beginning of the school year. That year, 110 million books were distributed, i.e., 83% more than in 1994. The books for 1997 began to be distributed in October 1996. By January 1997, some 87.2 million books had been delivered to 175,000 schools. Thus, all the children in the first to eighth grades in the public schools are being supplied books at the same time.

The FAE/FNDE, responsible for the program, is decentralizing the purchase and distribution of textbooks.

The School
Lunch Program
– to serve 34
million children

Created four decades ago, the National School Lunch Program gained new momentum in September 1995 when the Foundation for Student Assistance (FAE) increased by 50% the resources for buying foodstuffs. The nutritive level was increased for the snacks given to students, before classes begin, in the schools of the cities covered by the Community Solidarity Program.

SCHOOL LUNCH PROGRAM

Year	Municipalities	Students
1994	1,680	—
1995	3,912	33,262,484
1996	4,208	33,667,261

Source: MEC

The TV School Program – reaching 1.5 million teachers and 24 million students

The TV School Program broadcasted since March 1996 is an exclusive channel that, broadcast via satellite, reaches 51,820 schools throughout the country. Its programs both train and update teachers, and provide materials for classroom use. Every public school with more than one hundred students has received R\$1,500 to purchase the necessary equipment (television, VCR, antenna, table, and a box of ten VHS tapes).

A total of 38,846 schools have already purchased the equipment and 29,433 have installed it.

The computerization of education – 100,000 computers in 6,000 schools.

It is essential for the country to modernize its educational system with the introduction of computers. By the end of 1997, the first computers will be arriving at the public schools. In the meantime, teachers will be learning how to utilize the machines. Some R\$207,000,000 will be spent to train 25,000 teachers by the end of 1998. No school will receive computers unless it has teachers who are able to use them.

The State Secretaries of Education, using criteria based on the number of schools and the number of students in each of them, have selected the 6,000 schools that will receive 100,000 computers in the first phase of the Computerization Program.

XI. HOUSING AND SANITATION

The government has been preparing a genuine "revolution" for this area. Such revolution is based on a change in the manner of spending resources, which previously were disbursed directly to companies, states and cities for large-scale projects. In the past, large amounts of money were spent without producing much result.

The manner of channeling these funds was changed by creating a mechanism better suited to meeting the individual demands of the lowest income sectors. Multiple mechanisms were created to satisfy the demand of the public rather than just the demand of large companies.

The federal government, with just the investments made in 1995 and 1996, will directly benefit 3.9 million families throughout the country, facilitating the creation of 646,000 new jobs. In all, R\$4.8 billion have been invested in 3,078 projects in 2,400 municipalities. Of these projects, 900 have been concluded and 2,178 are underway.

The budget this year is R\$6.3 billion. These funds will benefit an estimated 5.2 million families and will create 1.2 million jobs.

Sanitation

When the government took office in January 1995, 9.62% of the urban houses were not supplied with treated water. With what the federal government has spent in this sector, including the counterpart funds of the states and cities, 788 projects have already been initiated in 644 municipalities. When these projects are completed, the percentage of urban houses without treated water will have been cut in half: from 9.62% to 4.82%.

The investments made during 1995 and 1996 on urban sewage systems are benefiting 6.8 million Brazilian families. With these outlays,

the government is reducing by 18.5% the number of residences in the country that lack sewage services. Only a little more than 20% of houses will still lack sewage services.

Housing

Just as the *Real Plan* was fundamental to the resumption of investment in sanitation, creating the conditions to medium- and long-term planning, it was also of great importance for housing. It caused a major increase in the purchasing power of the population, especially of the lowest income sectors, and it reestablished credit facilities. The principal indicator of this beneficial effect is the increase in the sales of such housing construction materials as cement and asbestos shingles and tubing.

The federal government housing policy also made possible progress in reducing the enormous housing shortage, either through the construction of new housing or through improvements in units that had deteriorated.

For the programs financed with resources of the FGTS or through the federal government budget, the Secretary of Urban Policy in the Ministry of Planning allocated R\$2 billion, including counterpart funds, during 1995 and 1996. These resources funded the construction of 83,000 housing units, the grant of 63,500 credit lines, and contracts for 400 other works. These programs will benefit 273,300 families and will allow the creation of 90,100 new jobs. The resources of just the Pro-Housing Program and Habitat-Brazil, designed for families with incomes of up to three minimum salaries, will allow the signing of 234 contracts for urban improvements in shanty towns and poor neighborhoods. These contracts will benefit almost 99,000 families. Moreover, these programs will undertake 147 housing and infrastructure projects. When these projects are complete, they will benefit more than 27,000 families.

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Secretaria de Comunicação Social

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