Prospectus Supplement to Prospectus dated July 19, 1999.

$1,000,000,000

Federative Republic of Brazil

12.75% U.S. Dollar-Denominated Global Bonds due 2020

Brazil will pay interest on the global bonds on January 15 and July 15 of each year. The first such payment will be made on July 15, 2000. The global bonds will be issued only in denominations of $1,000 and integral multiples of $1,000.

Application has been made to list the global bonds on the Luxembourg Stock Exchange.

Neither the Securities and Exchange Commission nor any other regulatory body has approved or disapproved of these securities or passed upon the accuracy or adequacy of this prospectus. Any representation to the contrary is a criminal offense.

	Per Global Bond	Total
Initial public offering price	96.394%	$963,940,000
Underwriting discount	.875%	$ 8,750,000
Proceeds, before expenses, to Brazil	95.519%	$955,190,000

The initial public offering price set forth above does not include accrued interest, if any. Interest on the global bonds will accrue from January 26, 2000 and must be paid by the purchaser if the global bonds are delivered after January 26, 2000.

The underwriters expect to deliver the global bonds in book-entry form only through the facilities of The Depository Trust Company against payment in New York, New York on January 26, 2000.

Chase Securities Inc. **Goldman, Sachs & Co.**

Prospectus Supplement dated January 19, 2000.

You should rely only on the information contained in or incorporated by reference in this prospectus supplement and the accompanying prospectus. Brazil has not authorized anyone to provide you with different information. Brazil is not making an offer of these securities in any state where the offer is not permitted. You should not assume that the information provided by this prospectus supplement or the accompanying prospectus is accurate as of any date other than the date on the front of this prospectus supplement.

ABOUT THIS PROSPECTUS SUPPLEMENT

Brazil, having made all reasonable inquiries, confirms that this prospectus supplement and the accompanying prospectus contain all information with respect to Brazil and the global bonds which is material in the context of the issue and offering of the global bonds, and that such information is true and accurate in all material respects and is not misleading, that the opinions and intentions expressed herein are honestly held and that, to the best of Brazil's knowledge and belief, there are no other facts the omission of which would make any such information or the expression of any such opinions and intentions materially misleading. Brazil accepts responsibility accordingly.

You should rely only on the information provided or incorporated by reference in this prospectus supplement and the accompanying prospectus. Brazil has not authorized anyone else to provide you with any other information. You should not rely on any other information in making your investment decision.

Brazil is not offering to sell or soliciting offers to buy any securities other than the global bonds offered under this prospectus supplement, nor is Brazil offering to sell or soliciting offers to buy the global bonds in places where such offers are not permitted by applicable law. You should not assume that the information in this prospectus supplement or the accompanying prospectus, or the information Brazil has previously filed with the Securities and Exchange Commission (the "Commission") and incorporated by reference in this prospectus supplement and the accompanying prospectus, is accurate as of any date other than their respective dates. Brazil's economic, fiscal or political circumstances may have changed since such dates.

The global bonds described in this prospectus supplement are debt securities of Brazil being offered under registration statement no. 333-10596 filed with the Commission under the U.S. Securities Act of 1933; the accompanying prospectus is part of the registration statement. The accompanying prospectus provides you with a general description of the securities that Brazil may offer, and this prospectus supplement contains specific information about the terms of this offering and the global bonds. This prospectus supplement also adds, updates or changes information provided or incorporated by reference in the accompanying prospectus. Consequently, before you invest, you should read this prospectus supplement together with the accompanying prospectus, as well as the documents incorporated by reference in this prospectus supplement and the accompanying prospectus. Those documents (such as Brazil's annual report on Form 18-K, which was filed on September 28, 1999) contain information regarding Brazil, the global bonds and other matters. The registration statement, any post-effective amendments thereto, the various exhibits thereto, and the documents incorporated therein by reference, contain additional information about Brazil and the global bonds. All such documents may be inspected at the office of the Commission. Certain terms used but not defined in this prospectus supplement are defined in the prospectus.

References to "U.S.$" or "$" in this prospectus supplement are to U.S. dollars.

The distribution of this prospectus supplement and the accompanying prospectus and the offering of the global bonds in certain jurisdictions may be restricted by law. Persons who receive copies of this prospectus supplement and the accompanying prospectus should inform themselves about and observe any such restrictions. See "Underwriting" in this prospectus supplement.

Brazil is a foreign sovereign state. Consequently, it may be difficult for investors to obtain or realize upon judgments of courts in the United States against Brazil. See "Arbitration and Enforceability" in the accompanying prospectus.

FORWARD-LOOKING STATEMENTS

Brazil has made forward-looking statements in this document. Statements that are not historical facts are forward-looking statements. These statements are based on Brazil's current plans, estimates, assumptions and projections. Therefore, you should not place undue reliance on them. Forward-looking statements speak only as of the date they are made, and Brazil undertakes no obligation to update any of them in light of new information or future events.

Forward-looking statements involve inherent risks. Brazil cautions you that many factors could affect the future performance of the Brazilian economy. These factors include, but are not limited to:

- External factors, such as:
  - interest rates in financial markets outside Brazil;
  - impact of changes in the credit rating of Brazil; and
  - decisions of international financial institutions, such as the International Monetary Fund, regarding the terms of their financial assistance to Brazil.
- Internal factors, such as:
  - general economic and business conditions in Brazil;
  - present and future exchange rates of the Brazilian currency;
  - foreign currency reserves;
  - ability of the Brazilian Government to enact key economic reforms;
  - level of domestic debt;
  - domestic inflation;
  - level of foreign direct and portfolio investment; and
  - level of Brazilian domestic interest rates.

SUMMARY OF THE OFFERING

The following summary is qualified in its entirety by, and should be read in conjunction with, the more detailed information appearing elsewhere in this prospectus supplement and the accompanying prospectus.

Issuer: Federative Republic of Brazil

Title of Security: 12.75% U.S. Dollar-Denominated Global Bonds due 2020

Aggregate Principal Amount: $1,000,000,000

Maturity Date: January 15, 2020

Interest Rate: 12.75% per annum

Interest Payment Dates: January 15 and July 15 of each year, starting July 15, 2000

Price to Public: 96.394% of principal amount

Form: Brazil will issue the global bonds in the form of one or more book-entry securities in fully registered form, without coupons. Brazil will not issue the global bonds in bearer form.

Denominations: Brazil will issue the global bonds in denominations of $1,000 and integral multiples of $1,000.

Payment of Principal and Interest: Principal and interest on the global bonds will be payable in U.S. dollars or other legal tender, coin or currency of the United States of America.

Status: The global bonds will rank equal in right of payment with all of Brazil's existing and future unsecured and unsubordinated external indebtedness.

Negative Pledge: The global bonds will contain certain covenants, including restrictions on the incurrence of certain liens.

Default: The global bonds will contain events of default, the occurrence of which may result in the acceleration of Brazil's obligations under the global bonds prior to maturity.

Listing: Application has been made to list the global bonds on the Luxembourg Stock Exchange.

Fiscal Agent: The global bonds will be issued pursuant to a fiscal agency agreement, dated as of November 1, 1996, between Brazil and The Chase Manhattan Bank, as fiscal agent, paying agent, transfer agent and registrar.

Taxation: For a discussion of the Brazilian and United States tax consequences associated with the global bonds, see "Taxation—Brazilian Taxation" and "—United States Federal Income and Estate Taxation" in this prospectus supplement and "Debt Securities—Payment of Additional Amounts" in the accompanying prospectus. Investors should consult their own tax advisors in determining the foreign, United States federal, state, local and any other tax consequences to them of the purchase, ownership and disposition of the global bonds.

Governing Law: The global bonds will be governed by the laws of the State of New York, except with respect to the authorization and execution of the global bonds, which will be governed by the laws of the Federative Republic of Brazil.

USE OF PROCEEDS

The net proceeds from the sale of the global bonds will be approximately $955,015,000, after deduction of expenses estimated to be $175,000 and the underwriting discount. The net proceeds will be used to refinance Brazil's internal debt at a lower cost and for a longer term.

RECENT DEVELOPMENTS

The information included in this section supplements the information about Brazil contained in Brazil's annual report for 1998 on Form 18-K filed with the Commission on September 28, 1999, as amended. To the extent the information in this section is inconsistent with the information contained in such annual report, the information in this section replaces such information. Initially capitalized terms not defined in this section have the meanings ascribed to them in that annual report. Cross-references in this section are to sections in that annual report.

Recent Economic Developments

On October 28, 1998, the Government announced a set of measures, collectively referred to as the Fiscal Stabilization Program, that included, among other things, (i) a proposal to extend the term of the Fiscal Stabilization Fund (FEF) to 2006 and increase the amount retained by the Government from the present 20% of certain tax revenues to 40% of such tax revenues and (ii) a proposal to extend to retired civil servants the obligation to make social security contributions in respect of their monthly pensions at tax rates ranging from 11% to 25% of the amount of their monthly pensions and increase the social security contribution of active civil servants earning more than R$1,200 per month for a period of five years. See "Introduction" and "The Brazilian Economy—*Plano Real* and Current Economic Policy". The Government subsequently elected not to seek an extension of the FEF or an increase of the amounts retained by the Government thereunder, and the FEF therefore expired on December 31, 1999. However, in January 1999, the National Congress approved legislation providing for social security contributions by retired civil servants and increases in social security contributions made by retired civil servants.

On September 30, 1999, the Federal Supreme Court of Brazil held the social security legislation unconstitutional. The Government estimates that the lost revenue resulting from the Federal Supreme Court's decision will total approximately R$2.38 billion in 2000. To compensate for the lost revenue, the Government announced on October 7, 1999 that it would reduce expenditures by R$1.2 billion and eliminate the tax deduction that corporations were permitted to take for the recent 1% increase in the COFINS rate. The combined additional revenue and cost savings are expected to total approximately R$2.38 billion during the following twelve-month period. The Government has also announced that it was considering the implementation of, among other things, a provisional measure to increase taxes on remittances for the payment of interest and other amounts in respect of external contractual obligations, the continuation of efforts to seek passage of the Fiscal Responsibility Law, previously announced tax reform proposals and a constitutional amendment to alter the revenue-sharing system between the Government and the States under the Constitution.

On October 6, 1999, the Chamber of Deputies approved, by a margin of 301 to 157, a bill that would change the rules for retirement for private sector employees. The bill introduces a new social security factor that will be used to calculate benefits for retirees. This factor takes into account not only age and years of contributions to the National Social Security Institute (*Instituto Nacional de Seguro Social* or INSS), but also life expectancy. The legislation also changes the base for calculating the INSS benefit of any retiree to the arithmetic mean of the monthly salaries of that retiree during 80% of the monthly periods since July 1994 when that monthly salary was highest, rather than the average monthly salary of that retiree during the last 36 months before retirement. The new social security factor is to be phased in over a five-year period. The bill must be approved by the Brazilian Senate and signed by the President before it becomes law.

On October 12, 1999, Brazil repaid approximately $1.477 billion to the Bank for International Settlements and the Ministry of Finance of Japan, representing approximately 30% of the second disbursement under the $41.8 billion IMF-led support plan, together with approximately $258 million in accrued interest. The remaining 70% was rolled over for another six months.

The December 1999 floor for net adjusted international reserves under the IMF-led support program was adjusted in October 1999 to $20.3 billion from $22.3 billion. Net adjusted international reserves are defined as gross reserves (balance of payments concept) less outstanding liabilities under the IMF-led support package. The reduction in the December 1999 floor was intended to give the Central Bank additional flexibility that month to intervene in the foreign exchange market.

Foreign Trade; International Reserves

On October 29, 1999, Brazil and Argentina signed a protocol under the Treaty of Asunciόn to give effect to a memorandum of understanding between institutions in the two countries responsible for the certification of products that harmonizes the two countries' standards for certification of certain products. The agreement covers a variety of products, including shoes, home appliances and toys.

During 1999, imports totaled $49.2 billion, a 14.8% reduction from 1998, while exports totaled $48.0 billion, a 6.1% reduction from the same period in 1998. Brazil's trade deficit for 1999 was approximately $1.2 billion.

At December 31, 1999, Brazil's international reserves stood at approximately $36.4 billion, corresponding to approximately 10 months of imports of goods.

Gross Domestic Product

During the first nine months of 1999, Brazil's GDP rose 0.02% compared to the same period in 1998.

Prices

The inflation rate, as measured by GPI-DS (the composite price index) declined to 7.48% in 1997 and 1.70% in 1998 from 9.34% in 1996. Since the Central Bank's decision to permit the value of the *real* to float, the inflation rate has increased, registering 19.68% for the twelve months ended November 1999.

Foreign Exchange

The *real*-dollar exchange rate (sell side) on December 31, 1999, as published by the Central Bank, was R$1.7890 to $1.00, up from R$1.9227 to $1.00 on November 30, 1999 and R$1.9530 to $1.00 on October 29, 1999.

During December 1999, the Central Bank has intervened in the foreign exchange markets to increase the liquidity of those markets to address concerns about the possible impact of Year 2000-related problems on external financing operations.

Unemployment; Labor

Unemployment rates rose during the first ten months of 1999, from 6.32% in December 1998 to 7.53% in October 1999.

On January 12, 2000, the National Congress enacted Law Nos. 9,957 and 9,958, which authorize labor court judges to issue final decisions in suits relating to labor disputes involving amounts in dispute not exceeding forty times the national minimum wage (currently R$136). The new laws do not apply to labor suits brought by Federal, state and municipal civil servants. Under Law No. 9,957, labor suits filed after March 14, 2000 against private and public corporations will be required to be decided within fifteen days. Currently, the average time for labor cases to be decided is five to seven years. If one of the parties challenges the labor judge's decision on the ground of insufficient evidence, a new hearing must be held within thirty days. Appeals of any decision may be made by employers or employees within ten days following the issuance of the decision. There is no time limit for higher labor courts to decide an appeal. In addition, Law No. 9,958 provides that companies can organize employers' and employees' commissions to resolve labor disputes before they are presented to the labor judge.

Public Debt

On November 4, 1999, the Government announced a set of measures intended to simplify Brazil's domestic securities market and to increase the liquidity of public sector debt securities. The proposed reforms include, among other things, a reduction in the number of maturities of government securities in the market, a reduction in the frequency of public offerings, an increase in the size of issues of long-term fixed-rate securities, the issuance by the Government of zero-coupon dollar-indexed securities and arrangements for the separate trading of the principal and interest components of such securities having a maturity of less than five years and the issuance of government debt securities in the SELIC book-entry system, with settlement of trades on the business day following the trade date.

At November 30, 1999, Brazil's U.S. dollar-indexed domestic securities debt totaled approximately R$98.4 billion, down from approximately R$100.5 billion at October 31, 1999.

At November 30, 1999, total external debt in Brazil stood at $238.9 billion. Of that amount, approximately $104.3 billion consisted of public sector external debt and approximately $134.6 billion consisted of private sector external debt. Interest expense on that debt amounted to approximately $14.1 billion (or 35.9% of exports) for the ten months ended October 31, 1999, of which approximately $6.6 billion (or 16.8% of exports) was paid in respect of public sector external debt and approximately $7.5 billion (or 19.1% of exports) was paid in respect of private sector external debt.

The Government completed an offering of Euro 500 million aggregate principal amount of its 11.125 per cent. Notes due 2004 on September 30, 1999, an offering of Euro 700 million aggregate principal amount of its 12.00 per cent. Notes due 2006 on November 17, 1999 and an offering of Euro 600 million aggregate principal amount of its 8.25 per cent. Notes due 2001 on November 26, 1999. On October 25, 1999, Brazil completed an exchange offer pursuant to which $2 billion aggregate principal amount of Brazil's 14.50% U.S. Dollar-Denominated Unsecured Global Bonds Due 2009 (the "2009 Bonds") were issued. Of this amount, approximately $177 million aggregate principal amount of the 2009 Bonds was issued in exchange for Par Bonds, approximately $519 million aggregate principal amount of the 2009 Bonds was issued in exchange for Front-Loaded Interest Reduction with Capitalization Bonds ("C-Bonds"), approximately $290 million aggregate principal amount of the 2009 Bonds was issued in exchange for Debt Conversion Bonds and approximately $1.014 billion aggregate principal amount of the 2009 Bonds was issued in exchange for Discount Bonds. Following the completion of the exchange offer, Brazil cancelled approximately

$299 million aggregate principal amount of Par Bonds, approximately $793 million aggregate principal amount of C-Bonds, approximately $449 million aggregate principal amount of Debt Conversion Bonds and approximately $1.462 billion aggregate principal amount of Discount Bonds acquired by Brazil in the exchange offer.

On December 9, 1999, Brazil received disbursements from the IMF totaling $1.1 billion under the November 1998 IMF-led support package. See "Introduction", "The Brazilian Economy—*Plano Real* and Current Economic Policy" and "Public Debt—External Debt". Brazil used the proceeds of the new loan and a portion of its international reserves to repay approximately $5.1 billion previously advanced under the support program. After giving effect to such disbursements and repayment, approximately $12.3 billion remained outstanding under the support program as of December 23, 1999.

On January 14, 2000, the Republic commenced an offering of Euro 750,000,000 aggregate principal amount of its 11.00 per cent. Notes due 2010. The net proceeds from the sale of the Notes, which are expected to be approximately Euro 733,800,000 before the payment of expenses relating to the offering, will be used to refinance internal debt of the Republic. None of the Notes is expected to be offered in the United States or to U.S. persons. The closing of the offering is subject to certain conditions.

DESCRIPTION OF THE GLOBAL BONDS

Brazil will issue the global bonds under the fiscal agency agreement, dated as of November 1, 1996, between Brazil and The Chase Manhattan Bank, as fiscal agent.

The following description is a summary of the material provisions of the global bonds and the fiscal agency agreement. Because it is only a summary, the description may not contain all of the information that is important to you as a potential investor in the global bonds. Therefore, Brazil urges you to read the fiscal agency agreement and the form of global bond in making your decision on whether to invest in the global bonds. Brazil has filed a copy of these documents with the Commission and will also file copies of these documents at the office of the fiscal agent in New York City.

The following description of the particular terms of the global bonds offered hereby supplements and replaces any inconsistent information set forth in the description of the general terms and provisions of the debt securities set forth in the prospectus.

General Terms of the Global Bonds

The global bonds will:

- be issued in an aggregate principal amount of $1,000,000,000.
- mature at par on January 15, 2020.
- bear interest at 12.75% from January 26, 2000.
- pay interest semi-annually in arrears in equal installments on January 15 and July 15 of each year, starting on July 15, 2000, to be paid to the person in whose name the global bond is registered at the close of business on the preceding December 31 or June 30.
- be direct, unconditional and general obligations of Brazil and will rank equal in right of payment with all of Brazil's payment obligations relating to its existing and future unsecured and unsubordinated external indebtedness.
- be recorded on, and transferred through, the records maintained by DTC and its direct and indirect participants, including Euroclear and Cedelbank.
- be issued in fully registered form, without coupons, registered in the names of investors or their nominees in denominations of $1,000 and integral multiples of $1,000.
- be available in definitive form only under certain limited circumstances.

Payment of Principal and Interest

Brazil will make payments of principal and interest on the global bonds in U.S. dollars to DTC, which will receive the funds for distribution to the beneficial holders of the global bonds. Brazil expects that holders of the global bonds will be paid in accordance with the procedures of DTC and its direct and indirect participants. Neither Brazil nor the paying agent will have any responsibility or liability for any aspect of the records of, or payments made by, DTC or any failure on the part of DTC in making payments to holders of the global bonds from the funds it receives.

Brazil, through DTC, will make its interest and principal payments to you, as a holder, by wire transfer if:

- you own at least $1,000,000 aggregate principal amount of the global bonds; and

- not less than 15 days before the payment date, you notify the fiscal agent of your election to receive payment by wire transfer and provide it with your bank account information and wire transfer instructions;

OR

- Brazil, through DTC, is making such payments at maturity; and
- you surrender the global bonds at the corporate trust office of the fiscal agent or at the offices of the other paying agents that Brazil appoints pursuant to the fiscal agency agreement.

If Brazil does not pay interest by wire transfer for any reason, it will, subject to applicable laws and regulations, mail a check to you on or before the due date for the payment at your address as it appears on the security register maintained by the fiscal agent on the applicable record date.

If any date for an interest or principal payment is a day on which the law at the place of payment permits or requires banking institutions to close, Brazil will make the payment on the next banking day at such place. Brazil will treat such payments as if they were made on the due date, and no interest on the global bonds will accrue as a result of this delay in payment.

If any money that Brazil pays to the fiscal agent for the payment of principal of or interest on the global bonds is not claimed at the end of two years after the principal or interest was due and payable, the fiscal agent will repay the money to Brazil. After any such repayment, the fiscal agent will not be liable with respect to the payments. However, Brazil's obligations to pay the principal of and interest on the global bonds as they become due will not be affected by such repayment. The global bonds will become void unless presented for payment within five years after the maturity date (or a shorter period if provided by applicable law).

Trading of the Global Bonds

The global bonds will be a new issue of securities with no established trading market. The underwriters have advised Brazil that they intend to make a market in the global bonds. They are not, however, obligated to do so and may discontinue their market-making activities at any time and without giving notice to Brazil. No assurance can be given that a trading market for the global bonds will develop, or as to the liquidity of the trading market if it does develop.

You should be aware that it is not possible to predict the price at which the global bonds will trade in the secondary market. The value of the global bonds will depend on, among other things, prevailing interest rates.

Paying Agents and Transfer Agents

Until the global bonds are paid, Brazil will maintain a paying agent in New York City. Brazil has initially appointed The Chase Manhattan Bank to serve as its paying agent and transfer agent in New York City.

In addition, so long as the global bonds are listed on the Luxembourg Stock Exchange and the rules of such exchange so require, Brazil will maintain a paying agent and transfer agent in Luxembourg. Brazil has initially appointed Chase Manhattan Bank Luxembourg S.A. to serve as its Luxembourg paying agent and transfer agent.

Brazil may at any time appoint new paying agents and transfer agents. Brazil will promptly provide notice (as described under "—Notices") of the termination or appointment of, or of any change in the office of, any paying agent or transfer agent.

Definitive Global Bonds

Brazil will issue global bonds in definitive form in exchange for the book-entry securities only if:

- DTC notifies Brazil that it is unwilling, unable or no longer qualified to continue to act as depositary and Brazil does not appoint a successor depositary within 90 days; or
- at any time Brazil decides it no longer wishes to have all or part of the global bonds represented by a book-entry security.

If Brazil issues definitive securities, they will have the same terms and authorized denominations as the book-entry security. You may present definitive securities for transfer or exchange at the corporate trust office of the fiscal agent in New York City, or at the office of the Luxembourg transfer agent, according to the procedures in the fiscal agency agreement. You will not be charged a fee for the registration of transfers or exchanges of definitive securities. You may, however, be charged for any stamp, tax or other governmental charge that must be paid in connection with the transfer, exchange or registration. Brazil, the fiscal agent and any other agent of Brazil may treat the person in whose name any definitive security is registered as the owner of such security for all purposes.

If any definitive security becomes mutilated, destroyed, stolen or lost, you can have it replaced by delivering the definitive security or the evidence of its loss, theft or destruction to the fiscal agent or the Luxembourg transfer agent. Brazil and the fiscal agent may require you to sign an indemnity under which you agree to pay Brazil, the fiscal agent or any other agent of Brazil for any losses that they may suffer relating to the definitive security that was mutilated, destroyed, stolen or lost. Brazil and the fiscal agent may also require you to present other documents or proof. After you deliver these documents, if neither Brazil nor the fiscal agent have notice that a *bona fide* purchaser has acquired the definitive security you are exchanging, Brazil will execute, and the fiscal agent will authenticate and deliver to you, a substitute definitive security with the same terms as the definitive security you are exchanging. You will be required to pay all expenses and reasonable charges associated with the replacement of the mutilated, destroyed, stolen or lost definitive security.

Notices

Brazil will publish notices to the holders of the global bonds in a leading newspaper having general circulation in London and New York. Brazil expects that it will make such publication in the *Financial Times* and *The Wall Street Journal*. So long as the global bonds are listed on the Luxembourg Stock Exchange and the rules of that exchange so require, Brazil will also publish notices to the holders of the global bonds in a leading newspaper having general circulation in Luxembourg. Brazil expects that it will initially make such publication in the *Luxemburger Wort*. If publication in a leading newspaper in Luxembourg is not practicable, Brazil will publish such notices in one other leading English language daily newspaper with general circulation in Europe. Brazil will consider a notice to be given on the date of its first publication.

In the case of the book-entry securities, notices also will be sent to DTC or its nominee, as the holder thereof, and DTC will communicate such notices to DTC participants in accordance with its standard procedures.

Further Issues of the Global Bonds

Brazil may, without the consent of holders of the global bonds, create and issue additional debt securities with the same terms and conditions as those of the global bonds (or the same except for the amount of the first interest payment and the issue price). Brazil may also consolidate the additional debt securities to form a single series with the outstanding global bonds.

GLOBAL CLEARANCE AND SETTLEMENT

Brazil has obtained the information in this section from sources it believes to be reliable, including from DTC, Euroclear and Cedelbank, and Brazil takes responsibility for the accurate reproduction of this information. Brazil takes no responsibility, however, for the accuracy of this information. DTC, Euroclear and Cedelbank are under no obligation to perform or continue to perform the procedures described below, and they may modify or discontinue them at any time. Neither Brazil nor the registrar will be responsible for DTC's, Euroclear's or Cedelbank's performance of their obligations under their rules and procedures. Nor will Brazil or the registrar be responsible for the performance by direct or indirect participants of their obligations under their rules and procedures.

Introduction

The Depository Trust Company

DTC is:

- a limited-purpose trust company organized within the meaning of the New York Banking Law;
- a "banking organization" under the New York Banking Law;
- a member of the Federal Reserve System;
- a "clearing corporation" within the meaning of the New York Uniform Commercial Code; and
- a "clearing agency" registered under Section 17A of the U.S. Securities Exchange Act of 1934.

DTC was created to hold securities for its participants and facilitate the clearance and settlement of securities transactions between its participants. It does this through electronic book-entry changes in the accounts of its direct participants, eliminating the need for physical movement of securities certificates. DTC is owned by a number of its direct participants and by the New York Stock Exchange, Inc., the American Stock Exchange and the National Association of Securities Dealers, Inc.

Euroclear and Cedelbank

Like DTC, Euroclear and Cedelbank hold securities for their participants and facilitate the clearance and settlement of securities transactions between their participants through electronic book-entry changes in their accounts. Euroclear and Cedelbank provide various services to their participants, including the safekeeping, administration, clearance and settlement, and lending and borrowing of internationally traded securities. Euroclear and Cedelbank participants are financial institutions such as underwriters, securities brokers and dealers, banks, trust companies and other organizations. The underwriters are participants in Euroclear or Cedelbank. Other banks, brokers, dealers and trust companies have indirect access to Euroclear or Cedelbank by clearing through or maintaining a custodial relationship with Euroclear or Cedelbank participants.

Ownership of the Global Bonds through DTC, Euroclear and Cedelbank

Brazil will issue the global bonds in the form of one or more fully registered book-entry securities, registered in the name of Cede & Co., a nominee of DTC. Financial institutions, acting as direct and indirect participants in DTC, will represent your beneficial interests in the book-entry securities. These financial institutions will record the ownership and transfer of your beneficial interests through book-entry accounts. You may hold your beneficial interests in the book-entry securities through Euroclear or Cedelbank, if they are participants in such systems, or indirectly through organizations that are participants in such systems. Euroclear and Cedelbank will hold their participants' beneficial interests in the book-entry securities in their customers' securities accounts with their depositaries. These depositaries of Euroclear and Cedelbank in turn will hold such interests in their customers' securities accounts with DTC.

Brazil and the fiscal agent generally will treat the registered holder of the global bonds, initially Cede & Co., as the absolute owner of the global bonds for all purposes. Once Brazil and the fiscal agent make payments to the registered holders, Brazil and the fiscal agent will no longer be liable on the global bonds for the amounts so paid. Accordingly, if you own a beneficial interest in the book-entry securities, you must rely on the procedures of the institutions through which you hold your interests in the book-entry securities (including DTC, Euroclear, Cedelbank, and their participants) to exercise any of the rights granted to the holder of the book-entry securities. Under existing industry practice, if you desire to take any action that Cede & Co., as the holder of such book-entry securities, is entitled to take, then Cede & Co. would authorize the DTC participant through which you own your beneficial interest to take such action, and that DTC participant would then either authorize you to take the action or act for you on your instructions.

DTC may grant proxies or authorize its participants (or persons holding beneficial interests in the global bonds through such participants) to exercise any rights of a holder or take any other actions that a holder is entitled to take under the fiscal agency agreement or the global bonds. Euroclear's or Cedelbank's ability to take actions as a holder under the global bonds or the fiscal agency agreement will be limited by the ability of their respective depositaries to carry out such actions for them through DTC. Euroclear and Cedelbank will take such actions only in accordance with their respective rules and procedures.

You may incur fees for the maintenance and operation of the book-entry accounts with the clearing systems in which your beneficial interests are held.

Transfers Within and Between DTC, Euroclear and Cedelbank

Since the purchaser determines the place of delivery, it is important for you to establish at the time of the trade where both the purchaser's and seller's accounts are located to ensure that settlement can be on the desired value date. Although DTC, Euroclear and Cedelbank have agreed to the following procedures in order to facilitate transfers of interests in the book-entry security among participants of DTC, Euroclear and Cedelbank, they are under no obligation to perform or continue to perform these procedures, and these procedures may be discontinued at any time. Neither Brazil nor the fiscal agent will have any responsibility for the performance by DTC, Euroclear or Cedelbank or their respective participants or indirect participants of their respective obligations under the rules and procedures governing their operations.

Trading Between DTC Purchasers and Sellers

DTC participants will transfer interests in the global bonds among themselves in the ordinary way according to DTC rules. DTC participants will pay for such transfers by wire transfer. The laws of some states require certain purchasers of securities to take physical delivery of the securities in definitive form. These laws may impair your ability to transfer beneficial interests in the global bonds to such purchasers. DTC can act only on behalf of its direct participants, who in turn act on behalf of indirect participants and certain banks. Thus, your ability to pledge beneficial interests in the global bonds to persons that do not participate in the DTC system, and to take other actions, may be limited because you will not possess a physical certificate that represents your interest.

Trading Between Euroclear and/or Cedelbank Participants

Participants in Euroclear and Cedelbank will transfer interests in the global bonds among themselves in the ordinary way according to the rules and operating procedures of Euroclear and Cedelbank.

Trading Between a DTC Seller and a Euroclear or Cedelbank Purchaser

When the global bonds are to be transferred from the account of a DTC participant to the account of a Euroclear or Cedelbank participant, the purchaser must first send instructions to Euroclear or Cedelbank through a participant at least one business day prior to the settlement date. Euroclear or Cedelbank will then instruct its depositary to receive the global bonds and make payment for them. On the settlement date, the depositary will make payment to the DTC participant's account and the global bonds will be credited to the depositary's account. After settlement has been completed, DTC will credit the global bonds to Euroclear or Cedelbank, Euroclear or Cedelbank will credit the global bonds, in accordance with its usual procedures, to the participant's account, and the participant will then credit the purchaser's account. These securities credits will appear the next day (European time) after the settlement date. The cash debit from the account of Euroclear or Cedelbank will be back-valued to the value date (which will be the preceding day if settlement occurs in New York). If settlement is not completed on the intended value date (*i.e.,* the trade fails), the cash debit will instead be valued at the actual settlement date.

Participants in Euroclear and Cedelbank will need to make funds available to Euroclear or Cedelbank in order to pay for the global bonds by wire transfer on the value date. The most direct way of doing this is to pre-position funds (*i.e.,* have funds in place at Euroclear or Cedelbank before the value date), either from cash on hand or existing lines of credit. Under this approach, however, participants may take on credit exposure to Euroclear and Cedelbank until the global bonds are credited to their accounts one day later.

As an alternative, if Euroclear or Cedelbank has extended a line of credit to a participant, the participant may decide not to pre-position funds, but to allow Euroclear or Cedelbank to draw on the line of credit to finance settlement for the global bonds. Under this procedure, Euroclear or Cedelbank would charge the participant overdraft charges for one day, assuming that the overdraft would be cleared when the global bonds were credited to the participant's account. However, interest on the global bonds would accrue from the value date. Therefore, in many cases the interest income on global bonds that the participant earns during that one-day period will substantially reduce or offset the amount of the participant's overdraft charges. Of course, this result will depend on the cost of funds (*i.e.,* the interest rate that Euroclear or Cedelbank charges) to each participant.

Since the settlement will occur during New York business hours, a DTC participant selling an interest in the global bonds can use its usual procedures for transferring global bonds to the depositaries of Euroclear or Cedelbank for the benefit of Euroclear or Cedelbank participants. The DTC seller will receive the sale proceeds on the settlement date. Thus, to the DTC seller, a cross-market sale will settle no differently than a trade between two DTC participants.

Trading Between a Euroclear or Cedelbank Seller and DTC Purchaser

Due to time zone differences in their favor, Euroclear and Cedelbank participants can use their usual procedures to transfer global bonds through their depositaries to a DTC participant. The seller must first send instructions to Euroclear or Cedelbank through a participant at least one business day prior to the settlement date. Euroclear or Cedelbank will then instruct its depositary to credit the global bonds to the DTC participant's account and receive payment. The payment will be credited in the account of the Euroclear or Cedelbank participant on the following day, but the receipt of the cash proceeds will be back-valued to the value date (which will be the preceding day if settlement occurs in New York). If settlement is not completed on the intended value date (*i.e.,* the trade fails), the receipt of the cash proceeds will instead be valued at the actual settlement date.

If the Euroclear or Cedelbank participant selling the global bonds has a line of credit with Euroclear or Cedelbank and elects to be in debit for the global bonds until it receives the sale proceeds in its account, then the back-valuation may substantially reduce or offset any overdraft charges that the participant incurs over that one-day period.

Finally, a day trader that uses Euroclear or Cedelbank and that purchases global bonds from a DTC participant for credit to a Euroclear or Cedelbank accountholder should note that these trades would automatically fail on the sale side unless affirmative action were taken. At least three techniques should be readily available to eliminate this potential problem:

- borrowing through Euroclear or Cedelbank for one day (until the purchase side of the day trade is reflected in its Euroclear or Cedelbank account) in accordance with the clearing system's customary procedures;
- borrowing the global bonds in the United States from a DTC participant no later than one day prior to settlement which would give the global bonds sufficient time to be reflected in the borrower's Euroclear or Cedelbank account in order to settle the sale side of the trade; or
- staggering the value dates for the buy and sell sides of the trade so that the value date for the purchase from the DTC participant is at least one day prior to the value date for the sale to the Euroclear or Cedelbank accountholder.

TAXATION

Brazilian Taxation

The following is a summary of certain Brazilian federal income taxation that may be relevant to a prospective non-Brazilian investor in the global bonds. The summary is based on Brazilian laws, rules and regulations in effect on the date of this prospectus supplement, all of which are subject to change, possibly with retroactive effect. This summary is not intended to constitute a complete analysis of the Brazilian income tax consequences to non-residents of Brazil of the purchase, receipt, ownership or disposition of the global bonds. This summary does not describe any of the tax consequences that may be applicable to residents of Brazil.

Prospective purchasers of the global bonds should consult their own tax advisors to determine the tax consequences arising from the purchase, ownership and disposition of the global bonds.

Unless a non-Brazilian holder of a global bond has some connection with Brazil other than the mere holding of a global bond or the receipt of principal or interest in respect of a global bond, payments of interest and principal on a global bond to that non-Brazilian holder will be made free and clear of, and without deduction for or on account of, Brazilian taxes.

Capital gains resulting from any trades of global bonds effected between or in respect of accounts maintained by or on behalf of non-residents of Brazil will not be subject to Brazilian income tax or other Brazilian taxes if these non-residents have no connection with Brazil other than as holders of an interest in the global bonds.

Payments of interest and principal on the global bonds to, and any gain realized upon the disposition of global bonds by, non-Brazilian holders of global bonds will not be subject to Brazilian estate tax.

United States Federal Income and Estate Taxation

The following is a summary of certain United States federal income and estate tax considerations that may be relevant to an initial holder of a global bond. This summary is based on U.S federal tax laws in effect on the date of this prospectus supplement. All of these laws and authorities are subject to change at any time, perhaps with retroactive effect. No assurances can be given that any changes in these laws or authorities will not affect the accuracy of the discussions set forth in this summary.

This summary deals only with holders that hold the global bonds as capital assets as defined in the United States federal tax laws. This summary does not address tax considerations applicable to:

- *investors who do not purchase the global bonds in the offering at the offering price;*
- *special classes of holders, such as dealers in securities or currencies, certain securities traders, banks, tax-exempt organizations and life insurance companies;*
- *traders in securities that elect to mark to market;*
- *persons that hold global bonds as part of a hedging transaction or a position in a straddle or conversion transaction; and*
- *persons whose functional currency is not the U.S. dollar.*

Prospective purchasers of global bonds should consult their own tax advisors concerning the consequences, in their particular circumstances, under the Code and the laws of any other taxing jurisdiction, of the ownership of global bonds.

Definition of United States Holder

A "United States Holder" is a holder of global bonds who or that is:

- a citizen or resident of the United States;
- a domestic corporation or partnership;
- an estate the income of which is subject to United States federal income tax without regard to its source; or
- a trust if a court within the United States is able to exercise primary supervision over the administration of such trust and one or more United States persons have the authority to control all substantial decisions of the trust.

United States Holders

The following discussion applies to you if you are a United States Holder.

Payments of Interest

Interest on a global bond will be taxable to a United States Holder as ordinary income at the time it is received or accrued, depending on the United States Holder's method of accounting for tax purposes.

Interest paid by Brazil on the global bonds will constitute income from sources outside the United States, but, with certain exceptions, will be "passive" or "financial services" income, which is treated separately from other types of income for purposes of computing the foreign tax credit allowable to a United States Holder under the United States federal income tax laws.

Purchase, Sale, Redemption and Retirement of the Global Bonds

A United States Holder's tax basis in a global bond will generally be its cost. A United States Holder will generally recognize capital gain or loss on the sale, redemption or retirement of a global bond equal to the difference between the amount realized (not including any amounts attributable to accrued but unpaid interest) on the sale, redemption or retirement and the holder's adjusted tax basis in the global bond. Such capital gain or loss will be long-term capital gain or loss if the global bond was held for more than one year. Under current law, net capital gains of individuals may be taxed at lower rates than items of ordinary income. The ability of a United States Holder to offset capital losses against ordinary income is limited. Any gain or loss recognized by a United States Holder on the sale, redemption or retirement of a global bond generally will be treated as income from sources within the United States or loss allocable to income from sources within the United States for United States federal income tax purposes.

Non-United States Holders

The following discussion applies to you if you are not a United States Holder (a "Non-United States Holder").

Interest on the Global Bonds

Subject to the discussion of backup withholding below, a Non-United States Holder will not be subject to United States federal income tax, including withholding tax, on payments of interest on the global bonds.

A Non-United States Holder, however, may be subject to United States federal income taxes on payments of interest on the global bonds if the Non-United States Holder:

- is an insurance company carrying on a U.S. insurance business to which the interest is attributable within the meaning of the United States federal tax laws; or
- has an office or other fixed place of business in the United States to which the interest is attributable and the interest is derived in the active conduct of a banking, financing or similar business within the United States.

Disposition of the Global Bonds

Subject to the discussion of backup withholding below, a Non-United States Holder will not be subject to United States federal income tax on any capital gain realized on the sale or exchange of the global bonds unless:

- that gain or income is effectively connected with the conduct by that Non-United States Holder of a trade or business within the United States; or
- in the case of a Non-United States Holder who is an individual, that Non-United States Holder is present in the United States for a total of 183 days or more during the taxable year in which that gain or income is realized, and either:
    - that gain is attributable to an office or fixed place of business maintained in the United States by that Non-United States Holder; or
    - that Non-United States Holder has a tax home in the United States.

Estate Tax

The global bonds will be treated as situated outside the United States for purposes of the United States federal estate tax. Thus, for purposes of that tax, the global bonds will not be included in the gross estate in the case of a nonresident of the United States who was not a citizen of the United States at the time of death.

Backup Withholding and Information Reporting

In general, information reporting requirements will apply to payments of principal of and interest on the global bonds to non-corporate United States Holders if those payments are made within the United States, or in the case of payments made after December 31, 2000, are made by or through a custodian or nominee that is a United States Controlled Person, as defined below. Backup withholding at a rate of 31% will apply to those payments if such a United States Holder fails to provide an accurate taxpayer identification number or, in the case of interest payments, fails to certify that it is not subject to backup withholding or is notified by the Internal Revenue Service that it has failed to report all interest and dividends required to be shown on its federal income tax returns.

The proceeds of a sale or redemption of global bonds effected at the U.S. office of a broker will generally be subject to the information reporting and backup withholding rules described above. In addition, the information reporting rules (and, in the case of payments made after December 31, 2000, other than payments to certain offshore accounts, the backup withholding rules) will apply to payments or proceeds of a sale or redemption effected at a foreign office of a broker that is a United States Controlled Person, unless the broker has documentary evidence that the holder or beneficial owner is not a United States Holder or the holder or beneficial owner otherwise establishes an exemption.

A "United States Controlled Person" is:

- a United States person (as defined in the United States Treasury regulations);

- a controlled foreign corporation for United States federal income tax purposes;
- a foreign person 50% or more of whose gross income is derived for tax purposes from a U.S. trade or business for a specified three-year period; or
- with respect to payments made after December 31, 2000, a foreign partnership in which United States persons hold more than 50% of the income or capital interests or which is engaged in a U.S. trade or business.

Any amounts withheld under the backup withholding rules from a payment to a holder of a global bond generally will be allowed as a refund or a credit against the holder's United States federal income tax liability as long as the holder provides the required information to the Internal Revenue Service.

UNDERWRITING

Brazil and the underwriters for the offering named below have entered into an underwriting agreement with respect to the global bonds. Subject to certain conditions, each underwriter has severally agreed to purchase the principal amount of the global bonds indicated in the following table:

Underwriters	Principal Amount of Global Bonds
Chase Securities Inc.	$ 500,000,000
Goldman, Sachs & Co.	$ 500,000,000
Total	$1,000,000,000

Global bonds sold by the underwriters to the public will initially be offered at the initial public offering price set forth on the cover of this prospectus supplement. If all global bonds are not sold at the initial offering price, the underwriters may change the offering price and the other selling terms.

The global bonds are a new issue of securities with no established trading market. Brazil has been advised by the underwriters that the underwriters intend to make a market in the global bonds but are not obligated to do so and may discontinue market making at any time without notice. No assurance can be given as to the liquidity of the trading market for the global bonds.

The global bonds are offered for sale in those jurisdictions in the United States, Europe and Asia where it is legal to make such offers. Only offers and sales of the global bonds in the United States, as part of the initial distribution thereof or in connection with resales thereof under circumstances where this prospectus supplement and the accompanying prospectus must be delivered, are made pursuant to the registration statement, of which the prospectus, as supplemented by this prospectus supplement, forms a part.

In connection with the offering, the underwriters may purchase and sell the global bonds in the open market. These transactions may include short sales, stabilizing transactions and purchases to cover positions created by short sales. Short sales involve the sale by the underwriters of a greater aggregate principal amount of global bonds than they are required to purchase in the offering. Stabilizing transactions consist of certain bids or purchases made for the purpose of preventing or retarding a decline in the market price of the global bonds while the offering is in progress.

The underwriters also may impose a penalty bid. This occurs when a particular underwriter repays to the underwriters a portion of the underwriting discount received by it because the representatives have repurchased global bonds sold by or for the account of such underwriter in stabilizing or short covering transactions.

These activities by the underwriters may stabilize, maintain or otherwise affect the market price of the global bonds. As a result, the price of the global bonds may be higher than the price that otherwise might exist in the open market. If these activities are commenced, they may be discontinued by the underwriters at any time. These transactions may be effected on the Luxembourg Stock Exchange, in the over-the-counter market or otherwise.

Brazil estimates that its share of the total expenses of this offering, excluding underwriting discounts and commissions, will be approximately $175,000.

Purchasers of the global bonds may be required to pay stamp taxes and other charges in accordance with the laws and practices of the country of purchase in addition to the price to the public set forth on the cover of this prospectus supplement.

The underwriters and their affiliates may engage in transactions with and perform services for Brazil. These transactions and services are carried out in the ordinary course of business.

Brazil has agreed to indemnify the several underwriters against certain liabilities, including liabilities under the Securities Act of 1933.

VALIDITY OF THE GLOBAL BONDS

The validity of the global bonds will be passed upon for Brazil by Dr. Almir Martins Bastos, the *Procurador-Geral da Fazenda Nacional* (Attorney General of the National Treasury), or, in his absence, a duly authorized Attorney of the National Treasury of the Republic and by Arnold & Porter, New York, New York, United States counsel to Brazil, and for the underwriters by Sullivan & Cromwell, New York, New York, United States counsel to the underwriters, and Pinheiro Neto-Advogados, São Paulo, SP, Brazilian counsel to the underwriters.

As to all matters of Brazilian law, Arnold & Porter may rely on the opinion of the Attorney General of the National Treasury or of such Attorney of the National Treasury, and Sullivan & Cromwell may rely on the opinion of Pinheiro Neto-Advogados. As to all matters of United States law, the Attorney General of the National Treasury or such Attorney of the National Treasury may rely on the opinion of Arnold & Porter and Pinheiro Neto-Advogados may rely on the opinion of Sullivan & Cromwell. Certain statements with respect to matters of Brazilian law in this prospectus supplement and the prospectus have been passed upon by the Attorney General of the National Treasury or, in his absence, a duly authorized Attorney of the National Treasury, and are made upon his authority.

OFFICIAL STATEMENTS AND DOCUMENTS

Information included in this prospectus supplement which is identified as being derived from a publication of, or supplied by, Brazil or one of its agencies or instrumentalities is included on the authority of that publication as a public official document of Brazil. All other information in this prospectus supplement is included as a public official statement made on the authority of Pedro Sampaio Malan, Minister of Finance.

GENERAL INFORMATION

Due Authorization

Brazil has authorized the creation and issue of the global bonds pursuant to Senate Resolution No. 57 of the Federal Senate of Brazil dated November 10, 1995, as amended by Senate Resolution No. 51 of the Federal Senate of Brazil dated June 10, 1997, and Senate Resolution No. 23 of June 29, 1999.

Listing and Listing Agent

Application has been made to list the global bonds on the Luxembourg Stock Exchange. The Luxembourg listing agent is Banque Internationale à Luxembourg S.A., 69, route d'Esch, L-1470 Luxembourg (Telephone: (352) 4590-3491).

Litigation

Neither Brazil nor any governmental agency of Brazil is involved in any litigation or arbitration or administrative proceeding relating to claims or amounts which are material in the context of the issue of the global bonds and which would materially and adversely affect Brazil's ability to meet its obligations under the global bonds and the fiscal agency agreement with respect to the global bonds. No such litigation or arbitration or administrative proceeding is pending, or, so far as Brazil is aware, threatened.

Documents Relating to the Global Bonds

Copies of the fiscal agency agreement and the form of global bond may be inspected during normal business hours on any weekday (Saturdays, Sundays and public holidays excepted) at the specified offices of the fiscal agent and paying agents.

Where You Can Find More Information

Brazil has filed its annual report for 1998 on Form 18-K (except for certain exhibits) with the Commission. You may request copies of this annual report, including its various exhibits, by contacting the Brazilian Embassy, 3006 Massachusetts Avenue, N.W., Washington, DC 20008, Attn: Finance Section (telephone: (202) 238-2745).

Each additional amendment to Form 18-K or each subsequent annual report on Form 18-K that Brazil files with the Commission after the date of this prospectus supplement but before the end of the offering of the global bonds is considered part of and incorporated by reference in this prospectus supplement. You may obtain a copy of all such documents, free of charge, at the office of the listing agent in Luxembourg.

Information on Brazil

If any global bonds are listed on the Luxembourg Stock Exchange, copies of the most recent *Boletim do Banco Central do Brasil* (the Bulletin of the Central Bank of Brazil), and (as or when available) each monthly publication thereof, or if the Bulletin of the Central Bank of Brazil ceases to be published, comparable economic information of *Banco Central do Brasil*, and any document incorporated by reference in this prospectus supplement may be obtained at the office of the listing agent for the global bonds and at the office of the fiscal agent during usual business hours on any day (Saturdays, Sundays and public holidays excepted).

Clearing

The global bonds have been accepted for clearance through DTC, Euroclear and Cedelbank (Common Code: 010616123; ISIN: US105756AK66; CUSIP No. 105756 AK 6).

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PROSPECTUS

FEDERATIVE REPUBLIC OF BRAZIL

$10,000,000,000

Debt Securities
Warrants

Brazil may offer up to $10,000,000,000 (or its equivalent in other currencies) aggregate principal amount of its debt securities with or without warrants to purchase debt securities.

Brazil may offer any combination of debt securities and/or warrants from time to time in one or more offerings. Brazil will provide specific terms of these securities in supplements to this prospectus. You should read this prospectus and any prospectus supplement carefully before you invest.

Brazil may sell the securities directly, through agents designated from time to time or through underwriters or dealers.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or determined whether this prospectus is accurate or complete. Any representation to the contrary is a criminal offense.

You should rely only on the information contained or incorporated by reference in this prospectus or any prospectus supplement. Brazil has not authorized anyone to provide you with different or additional information. Brazil is not making an offer of these debt securities or warrants in any place where the offer is not permitted by law. You should not assume that the information in this prospectus or any prospectus supplement or any document incorporated by reference is accurate as of any date other than the date on the front of those documents.

The date of this prospectus is July 19, 1999.

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WHERE YOU CAN FIND MORE INFORMATION

Brazil voluntarily files annual reports with the Securities and Exchange Commission (SEC). These reports and any amendments to these reports include certain financial, statistical and other information about Brazil, and may be accompanied by exhibits. You may read and copy any document Brazil files with the SEC at the SEC's public reference rooms in Washington, D.C., New York, New York and Chicago, Illinois. You may also obtain copies of the same documents from the public reference room in Washington by paying a fee. Please call the SEC at 1-800-SEC-0330 for further information on the public reference rooms.

The SEC allows Brazil to "incorporate by reference" the information Brazil files with it. This means that Brazil can disclose important information to you by referring you to those documents. Information that is incorporated by reference is an important part of this prospectus. Brazil incorporates by reference the following documents:

- Brazil's Annual Report on Form 18-K for the year ended December 31, 1997; and
- All amendments to Brazil's Annual Report on Form 18-K for the year ended December 31, 1997 filed prior to the date of this prospectus.

Brazil also incorporates by reference all future annual reports and amendments to annual reports until it sells all of the debt securities and warrants covered by this prospectus. Each time Brazil files a document with the SEC that is incorporated by reference, the information in that document automatically updates the information contained in previously filed documents.

You may request a free copy of these filings by writing or calling the Embassy of Brazil at the following address:

Embassy of Brazil
3006 Massachusetts Avenue, N.W.
Washington, D.C. 20008
Attn: Finance Section
(202) 238-2745

USE OF PROCEEDS

Unless otherwise specified in the applicable prospectus supplement, Brazil will use the net proceeds from the sale of the securities for the general purposes of Brazil, including the refinancing of domestic and external indebtedness of Brazil.

DEBT SECURITIES

Brazil may issue debt securities, with or without warrants, in distinct series at various times, and these debt securities will be issued pursuant to a fiscal agency agreement between Brazil and a fiscal agent. Brazil has filed a copy of the form of fiscal agency agreement as an exhibit to the registration statement (of which this prospectus is a part). The financial terms and other specific terms of a particular series of debt securities will be described in a prospectus supplement relating to such securities. If the terms or conditions described in the prospectus supplement that relate to your series of debt securities differ from the terms or conditions described in this prospectus, you should rely on the terms or conditions described in the prospectus supplement.

In this description of debt securities, you will see some initially capitalized terms. These terms have very particular, legal meanings, and you can find their definitions under the heading "Definitions" below.

General

The prospectus supplement that relates to your debt securities will specify the following terms:

- the specific title or designation of the debt securities;
- the principal amount of the debt securities;
- the price of the debt securities;
- the stated maturity date on which Brazil agrees to repay principal;
- the rate of any interest the debt securities will bear and, if variable, the method by which the interest rate will be calculated;
- the dates on which any interest payments are scheduled to be made;
- the date or dates from which any interest will accrue;
- the record dates for any interest payable on an interest payment date;
- whether and under what circumstances and terms Brazil may redeem the debt securities before maturity;
- whether and under what circumstances and terms the holders of the debt securities may opt to have their respective debt securities prepaid;
- the currency or currencies in which such debt securities are denominated, which may be U.S. dollars, another foreign currency or units of two or more currencies;
- the currency or currencies for which such debt securities may be purchased and in which principal, premium, if any, and interest may be payable;
- whether any amount payable in respect of the debt securities will be determined based on an index or formula, and, if so, how any such amount will be determined;
- whether the debt securities will be issued upon the exchange or conversion of other debt securities and, if so, the specific terms relating to this exchange or conversion;
- whether any part or all of the debt securities will be in the form of a global security and the circumstance in which a global security is exchangeable for certificated (physical) securities;
- whether the debt securities will be listed and if listed, the stock exchange on which these debt securities will be listed; and
- any other terms of the debt securities.

If applicable, the prospectus supplement may also describe any United States federal or Brazilian income tax consequences and special considerations applicable to that particular series of debt securities.

Any moneys held by the fiscal agent in respect of debt securities and remaining unclaimed for two years after those amounts have become due and payable shall be returned to Brazil. After the return of these moneys to Brazil, the holder of this debt security may look only to Brazil for any payment.

Brazil may replace the fiscal agent at any time, subject to the appointment of a replacement fiscal agent. The fiscal agent is an agent of Brazil and is not a trustee for the holders of the debt securities.

Status of the Debt Securities

The debt securities will be direct, unconditional and general obligations of Brazil. Except as described under the heading "Negative Pledge" below, the debt securities are unsecured obligations of Brazil. Brazil has pledged its full faith and credit for the due and punctual payment of principal of and interest on the debt securities.

The debt securities of any series will rank at least equally in right of payment with all other payment obligations relating to External Indebtedness.

Form of Debt Securities

Unless otherwise specified in the prospectus supplement, debt securities denominated in U.S. dollars will be issued:

- only in fully registered form;
- without interest coupons; and
- in denominations of $1,000 and greater multiples.

Debt securities denominated in another monetary unit will be issued in the denominations set forth in the applicable prospectus supplement.

Payment

Unless otherwise specified in the applicable prospectus supplement, principal of and interest on the debt securities will be payable in U.S. dollars at the New York office of the fiscal agent to the registered holders of the debt securities on the related record date; *provided, however,* unless otherwise specified in the prospectus supplement, interest will be paid by check mailed to the registered holders of the debt securities at their registered addresses.

The register of holders of debt securities will be kept at the New York office of the fiscal agent.

Negative Pledge

Brazil undertakes with respect to each series of debt securities that, as long as any debt securities of that series remain outstanding, it will not create or permit to subsist any Security Interest in any of its present or future revenues or properties to secure any Public External Indebtedness of Brazil, unless:

- the debt securities of that series are secured equally and ratably with that Public External Indebtedness; or
- the debt securities of that series have the benefit of another security, guarantee, indemnity or other arrangement as approved by the holders of the debt securities of that series as provided under the heading "Meetings and Amendments" below.

Notwithstanding the foregoing, Brazil may create or permit to subsist:

- Security Interests created prior to the date of issuance of the debt securities of a particular series, including renewals or refinancings of those Security Interests, *provided, however*, that any renewal or refinancing of any those Security Interests secures only the renewal or extension of the original secured financing;
- Security Interests created or contemplated under the agreements (as they may be amended from time to time) implementing the 1992 Financing Plan and explanatory communications relating to the 1992 Financing Plan and implementing documentation for the 1992 Financing Plan, including Security Interests to secure obligations under the Collateralized Bonds;
- Security Interests securing Public External Indebtedness of the Republic issued upon surrender or cancellation of any of the Collateralized Bonds or the principal amount of any Indebtedness of the Republic outstanding as of April 14, 1994, in each case, to the extent those Security Interests are created to secure that Public External Indebtedness on a basis comparable to the Collateralized Bonds;
- Security Interests securing Public External Indebtedness incurred or assumed by the Republic in connection with a Project Financing, *provided*, that the property over which those Security Interests are granted consists solely of assets or revenues of the

project for which the Project Financing was incurred;

- Security Interests securing Public External Indebtedness which
  - is issued by the Republic in exchange for debt of Brazilian public sector bodies (other than Brazil), and;
  - is in an aggregate principal amount outstanding that does not exceed $25,000,000 (or its equivalent in any other currency); and
- Security Interests securing Public External Indebtedness incurred or assumed by the Republic to finance or refinance the acquisition of the assets in which those Security Interests have been created or permitted to subsist.

Definitions

"1992 Financing Plan" means the Federative Republic of Brazil 1992 Financing Plan dated December 29, 1992 sent to the international banking community with the communication dated December 29, 1992 from the Minister of Finance of Brazil.

"Collateralized Bonds" means the collateralized bonds issued under the agreements (as they may be amended from time to time) implementing the 1992 Financing Plan.

"External Indebtedness" means any Indebtedness for money borrowed which is payable by its terms or at the option of its holder in any currency other than Brazilian currency (other than any such Indebtedness that is originally issued within Brazil).

"Indebtedness" means all unsecured, unsubordinated obligations of Brazil in respect of money borrowed and guarantees given by Brazil in respect of money borrowed by others.

"Public External Indebtedness" means any Public Indebtedness which is payable by its terms or at the option of its holder in any currency other than Brazilian currency (other than such Public Indebtedness that is originally issued within Brazil); settlement of original issuance by delivery of Public Indebtedness (or the instruments evidencing such Public Indebtedness) within Brazil shall be deemed to be original issuance within Brazil.

"Public Indebtedness" means any payment obligation, including any contingent liability, of any person arising from bonds, debentures, notes or other securities which:

- are, or were intended at the time of issuance to be, quoted, listed or traded on any securities exchange or other securities market (including, without limiting the generality of the foregoing, securities eligible for sale pursuant to Rule 144A under the United States Securities Act of 1933 (or any successor law or regulation of similar effect)); and
- have an original maturity of more than one year or are combined with a commitment so that the original maturity of one year or less may be extended at the option of Brazil to a period in excess of one year.

"Project Financing" means any financing of all or part of the costs of the acquisition, construction or development of any project and the person or persons providing such financing expressly agree to limit their recourse to the project financed and the revenues derived from such project as the principal source of repayment for the moneys advanced.

"Security Interest" means any lien, pledge, mortgage, security interest or other encumbrance.

Default; Acceleration of Maturity

Any of the following events will be an event of default with respect to any series of debt securities:

(a) a default by Brazil in any payment of principal of or interest on any debt securities of any series for 30 days;

(b) a default which is materially prejudicial to the interests of the holders of the debt securities of that series in the performance of any other obligation under the debt securities of that series, which continues for 30 days after the holder of any debt securities of that series provided to the fiscal agent written notice requiring this default be remedied;

(c) an acceleration of any aggregate principal amount of Public External Indebtedness of Brazil, which exceeds $25,000,000 (or its equivalent in any other currency), by reason of an event of default arising from Brazil's failure to make any payment of principal or interest under this Public External Indebtedness when due;

(d) a failure of Brazil to make any payment in respect of the Public External Indebtedness of Brazil in an aggregate principal amount in excess of $25,000,000 (or its equivalent in any other currency) when due (as such date may be extended by virtue of any applicable grace period or waiver), which continues for 30 days after the holder of any debt securities of that series provided to the fiscal agent written notice requiring this default be remedied;

(e) a declaration by Brazil of a moratorium with respect to the payment of principal of or interest on Public External Indebtedness of Brazil which does not expressly exclude the debt securities of that series and which is materially prejudicial to the interests of the holders of the debt securities of that series; or

(f) a denial or repudiation by Brazil of its obligations under the debt securities of that series.

If an event of default described above occurs, each holder of debt securities of any series may declare the principal of and any accrued interest on the debt securities it holds immediately due and payable; however, if an event of default described in clause (b), (c) or (d) above occurs (unless an event of default described in clause (a), (e) or (f) occurs at the time of receipt of the notice declaring the debt securities of that series due and payable), then any notice declaring the debt securities of that series due and payable becomes effective only when the fiscal agent has received these notices from holders of at least 10% in principal amount of all debt securities of that series then outstanding. Debt securities held directly by Brazil or on its behalf shall not be considered "outstanding" for this purpose.

Holders of debt securities may exercise these rights only by providing a written demand to Brazil and the fiscal agent at a time when the event of default is continuing.

If an event of default described in clause (a), (e) or (f) above ceases to continue, then each holder of debt securities of that series, which has declared its debt securities immediately due and payable, may rescind and annul this declaration. If an event of default described in clause (b), (c) or (d) above ceases to continue and no event of default described in clause (a), (e) or (f) above has occurred and is continuing, then all of the declarations that the debt securities are immediately due and payable may be rescinded and annulled by the affirmative vote of the holders of that series as provided under the heading "Meetings and Amendments" below.

Redemption and Repurchase

Unless otherwise set forth in the applicable prospectus supplement, the debt securities will not be redeemable prior to maturity at the option of Brazil or the registered holders of these debt securities.

Brazil may at any time purchase debt securities in any manner and for any consideration. These debt securities purchased by Brazil may, at its discretion, be held, resold or cancelled.

Meetings and Amendments

General. A meeting of holders of debt securities of any series may be called at any time:

- to make, give or take any request, demand, authorization, direction, notice, consent, waiver or other action provided for in the fiscal agency agreement or the debt securities of that series; or
- to modify, amend or supplement the terms of the debt securities of that series or the fiscal agency agreement.

Brazil may at any time call a meeting of holders of debt securities of a series for any purpose described above. This meeting will be held at the time and place determined by Brazil. If an event of default occurs and Brazil or the holders of at least 10% in aggregate principal amount of the outstanding debt securities of a series request (in writing) the fiscal agent to call a meeting, the fiscal agent will call such a meeting.

For the purpose of this section under the heading "Meetings and Amendments," "outstanding debt securities" does not include:

- previously canceled debt securities;
- debt securities called for redemption;

- debt securities which have become due and payable and for which sufficient funds to pay amounts owed under these debt securities have been paid or provided for;
- debt securities of a series, which have been substituted with another series of debt securities; and
- debt securities held directly by Brazil or on its behalf.

Notice. The notice of a meeting will set forth the time and place of the meeting and in general terms the action proposed to be taken at the meeting. This notice shall be given as provided in the terms of the debt securities. In addition, this notice shall be given between 30 to 60 days before the meeting date; however, in the case of any meeting to be reconvened after adjournment for lack of a quorum, this notice shall be given between 15 and 60 days before the meeting date.

Voting; Quorum. A person that holds outstanding debt securities of a series or is duly appointed to act as proxy for a holder of these debt securities will be entitled to vote at a meeting of holders of the debt securities of that series. The presence at the meeting of persons entitled to vote a majority of the principal amount of the outstanding debt securities shall constitute a quorum.

If a quorum is not present within 30 minutes of the time appointed for the meeting, the meeting may be adjourned for a period of at least 10 days as determined by the chairman of the meeting. If the meeting is convened at the request of the holders, however, then the meeting shall be dissolved.

In the absence of a quorum at a reconvening of a previously adjourned meeting, this meeting may be further adjourned for a period of at least 10 days as determined by the chairman of the meeting. Notice of the reconvening of an adjourned meeting shall be given only once. This notice shall state expressly the percentage of the principal amount of the outstanding debt securities of that series which shall constitute a quorum. Subject to the foregoing, at the reconvening of a meeting adjourned for a lack of a quorum, the presence of persons entitled to vote 25% in principal amount of the outstanding debt securities shall constitute a quorum for the taking of any action set forth in the notice of the original meeting.

In addition, any meeting at which a quorum is present may be adjourned by the vote of a majority of the principal amount of the outstanding debt securities of the series represented at the meeting, and the meeting may be held as so adjourned without further notice.

If a quorum is present at the meeting, any resolution and all matters shall be effectively passed or decided by the vote of the persons entitled to vote 66 ⅔% in aggregate principal amount of the outstanding debt securities of such series represented and voting at the meeting.

Regulations. The fiscal agent may make reasonable and customary regulations as it deems advisable for any meeting with respect to:

- the proof of the holding of debt securities of a series;
- the adjournment and chairmanship of such meeting;
- the appointment and duties of inspectors of votes, certificates and other evidence of the right to vote; and
- other matters concerning the conduct of the meeting that the fiscal agent deems appropriate.

Chairman. The fiscal agent will appoint a temporary chairman of the meeting by an instrument in writing. If Brazil or the holders of the debt securities of a series called the meeting, however, then Brazil or the holders calling the meeting, as the case may be, will appoint a temporary chairman by an instrument in writing.

A permanent chairman and a permanent secretary of the meeting shall be elected by the vote of the persons entitled to vote a majority of the principal amount of the outstanding debt securities of the series represented and voting at the meeting. The chairman of the meeting shall have no right to vote, except as a holder of debt securities of that series or proxy.

Record. A record, and at least one duplicate, of the proceedings of each meeting of holders will be prepared. One copy of the record of each meeting will be delivered to Brazil and another to the fiscal agent to be preserved by the fiscal agent.

Amendments. Unless the unanimous consent of holders of debt securities of an affected series is required as specified below, with:

- the affirmative vote, in person or by proxy, of the holders of at least 66 ⅔% in aggregate principal amount of the outstanding debt securities of a series represented and voting at a duly called and held meeting; or
- the written consent of the holders of 66 ⅔% in aggregate principal amount of the outstanding debt securities of a series:

(i) if both Brazil and the fiscal agent agree, they may modify, amend or supplement the terms of the debt securities of a series or, insofar as it affects the debt securities of that series, the fiscal agency agreement, in any way and (ii) holders of debt securities of a series may make, take or give any request, demand, authorization, direction, notice, consent, waiver or action provided by the fiscal agency agreement or the debt securities of such series to be made, given or taken by holders of debt securities of such series.

The written consent or affirmative vote of the holder of each debt security of an affected series is required to:

- change the due date for the payment of the principal of, or any installment of interest on, any debt security of such series;
- reduce the principal amount of any debt security of such series;
- reduce the portion of the principal amount which is payable in the event of an acceleration of the maturity of the debt security;
- reduce the interest rate on the debt security;
- change the currency in which any amount in respect of the debt securities of that series is payable;
- reduce the proportion of the principal amount of the debt securities of that series that is required:
  - to modify, amend or supplement the fiscal agency agreement or the terms and conditions of the debt securities of that series, or
  - to make, take or give any request, demand, authorization, direction, notice, consent, waiver or other action; or
- change the obligation of Brazil to pay additional amounts.

If both Brazil and the fiscal agent agree, they may, without the vote or consent of any holder of debt securities of a series, modify, amend or supplement the fiscal agency agreement or the debt securities of any series for the purpose of:

- adding to the covenants of Brazil;
- surrendering any right or power conferred upon Brazil;
- securing the debt securities of that series pursuant to the requirements of the debt securities or otherwise;
- correcting or supplementing any defective provision contained in the fiscal agency agreement or in the debt securities of that series; or
- amending the fiscal agency agreement or the debt securities of that series in any manner which Brazil and the fiscal agent may determine and that does not adversely affect the interest of any holder of debt securities of that series in any material respect.

Any modification, amendment or supplement approved in the manner described in this section shall be binding on the holders of debt securities of such series. Any modification, amendment or supplement approved in the manner described in this section shall be binding on the holders of debt securities of such series.

Judgment Currency

If a court or arbitral tribunal renders a judgment or order in respect of amounts due to a holder of a debt security and this judgment or order permits Brazil to pay those amounts in a currency (the "judgment currency") other than the currency in which the debt security is denominated (the "debt security currency"), Brazil will pay any deficiency arising or resulting from any variation in the rates of exchange between the date as of which the amount in the debt security currency is notionally converted into the amount in the judgment currency for the purposes of this judgment or order and the date of actual payment of this judgment or order.

Payment of Additional Amounts

All payments of principal and interest in respect of the debt securities by Brazil will be made free and clear of, and without withholding or deduction for or on account of, any present or future taxes, duties, assessments or governmental charges imposed, levied, collected, withheld or assessed by or within Brazil or any authority of or within Brazil having power to tax (together, "Taxes"), unless that withholding or deduction is required by law. In that event, Brazil shall pay those additional amounts that will result in receipt by the holders of debt securities of the amounts that would have been received by them had that withholding or deduction not been required, except that no additional amounts shall be payable with respect to any debt security:

- to a holder (or a third party on behalf of a holder) where that holder is liable to pay those Taxes in respect of any debt security by reason of that holder's having some connection with Brazil other than the mere holding of that debt security or the receipt of principal and interest in respect of that debt security;
- presented for payment more than 30 days after the Relevant Date (see below) except to the extent that the holder of that debt security would have been entitled to additional amounts on presenting the same for payment on the last day of that 30-day period; or
- to the extent that the Taxes to which those additional amounts relate would not have been imposed but for the failure of the holder or beneficial owners of that debt security to comply with any certification, identification or other reporting requirements concerning the nationality, residence or connection with Brazil or any political subdivision or taxing authority of or in Brazil (other than a requirement that has the effect of disclosing the nationality, residence or identity of a beneficial owner of that debt security to Brazil, any paying agency or any governmental authority), of that holder or beneficial owner, as a precondition to exemption from those Taxes.

The term "Relevant Date" in respect of any debt security means the later of:

- the date on which payment in respect of the debt security first becomes due and payable; or
- if the full amount of the money payable has not been received by the fiscal agent on or prior to that due date, the date on which notice is given to the holders of debt securities that the full amount of those moneys have been received and are available for payment. Any reference in this section to "principal" and/or "interest" includes any additional amounts which may be payable under the debt securities.

Global Securities

The prospectus supplement that relates to your debt securities indicates whether any of the debt securities you purchase will be represented by a global security. The aggregate principal amount of any global security equals the sum of the principal amount of all the debt securities it represents. The global security will be registered in the name of the depositary identified in the prospectus supplement or its nominee, and will be deposited with the depositary, its nominee or a custodian.

Limitations on Your Ability to Obtain Debt Securities Registered in Your Name. The global security will not be registered in the name of any person other than the depositary or its nominee. Similarly, the global security will not be exchanged for debt securities that are registered in the name of any person other than the depositary or its nominee. An exception to these restrictions would be made only if:

- the depositary notifies Brazil that it is unwilling, unable or no longer qualified to continue to act as depositary and Brazil does not appoint a successor depositary within 90 days; or
- at any time Brazil decides it no longer wishes to have all or part of the debt securities represented by a global security.

In those circumstances, the depositary will determine in whose names to register any certificated (physical) debt securities issued in exchange for the global security. These certificated (physical) debt securities will be issued:

- only in fully registered form;
- without interest coupons; and
- in denominations of $1,000 and greater multiples.

The depositary or its nominee will be considered the sole owner and holder of the global security for all purposes. As a result:

- You cannot get debt securities registered in your name for so long as they are represented by the global security;
- You cannot receive certificated (physical) debt securities in your name in exchange for your beneficial interest in the global security;
- You will not be considered to be the owner or holder of the global security or any debt securities represented by the global security for any purpose;
- You cannot assert any right of a holder of the debt securities unless you are authorized by the depositary and the participant through which you hold your beneficial interest; and
- All payments on the global security will be made to the depositary or its nominee.

In some jurisdictions, certain types of purchasers (such as some insurance companies) are not permitted to own securities represented by a global security. These laws may limit your ability to sell or transfer your beneficial interest in the global security to these types of purchasers.

Beneficial Interests in and Payments on Global Security. Institutions that have accounts with the depositary or a nominee of the depositary, such as securities brokers and dealers, are called participants. Only participants, and persons that hold beneficial interests through participants, can own a beneficial interest in the global security. The depositary keeps records of the ownership and transfer of beneficial interests in the global security by its participants. In turn, participants keep records of the ownership and transfer of beneficial interests in the global security by other persons (such as their customers). No other records of the ownership and transfer of beneficial interests in the global security will be kept.

When the depositary receives payment of principal or interest on the global security, the depositary is expected to credit its participants' accounts in amounts that correspond to their respective beneficial interests in the global security. In turn, after the participants' accounts are credited, the participants are expected to credit the accounts of the owners of beneficial interests in the global security in amounts that correspond to the owners' respective beneficial interests in the global security.

The depositary and its participants establish policies and procedures that govern payments, transfers, exchanges and other important matters that affect owners of beneficial interests in the global security. The depositary and its participants may change these policies and procedures from time to time. Brazil has no responsibility or liability for the records of owners of beneficial interests in the global security. Also, Brazil is not responsible for maintaining, supervising or reviewing those records or payments. Brazil has no responsibility or liability for any aspect of the relationship between the depositary and its participants or for any aspects of the relationship between participants and owners of beneficial interests in the global security.

WARRANTS

Brazil may issue warrants to purchase debt securities, either separately or together with debt securities. If Brazil issues any warrants, each issue of warrants will be issued under a warrant agreement between Brazil and a bank or trust company, as warrant agent. The terms of any warrant agreement related to the issue of warrants and the specific terms of the issue of warrants will be described in the prospectus supplement that relates to your particular warrants. The prospectus supplement that relates to your particular warrants will describe the following terms:

- the terms listed under the heading "Debt Securities" as they relate to the particular debt securities you have the right to purchase if you exercise your warrants;

- the amount of debt securities each warrant entitles you to purchase if you exercise your warrants and the purchase price of those debt securities;
- the procedures you must follow and the conditions you must satisfy to exercise your warrants;
- the dates on which your right to exercise your warrants begins and expires;
- whether and under what conditions Brazil may cancel or terminate your warrants;
- whether and when your warrants and any debt securities issued together with your warrants may be sold or transferred separately;
- whether the certificates that represent the warrants will be issued in registered or bearer form, whether they will be exchangeable as between such forms and, if issued in registered form, whether the warrants can be transferred and registered; and
- any special United States federal income tax considerations applicable to the issuance of your warrants; and
- any other terms of such warrants.

GOVERNING LAW

The fiscal agency agreement, the warrant agreement, the debt securities and the warrants will be governed by and interpreted in accordance with the laws of the State of New York, without regard to any conflicts-of-laws principles that would require the application of the laws of a jurisdiction other than the State of New York. The laws of Brazil will govern all matters concerning authorization and execution of the securities by Brazil.

ARBITRATION AND ENFORCEABILITY

Under Brazilian law, Brazil is prohibited from submitting to the jurisdiction of a foreign court for the purposes of adjudication on the merits in any dispute, controversy or claim against Brazil arising out of or relating to the securities. Brazil has agreed, however, that any dispute, controversy or claim arising out of or relating to the securities (other than any action arising out of or based on United States federal or state securities laws), including the performance, interpretation, construction, breach, termination or invalidity of the securities, shall be finally settled by arbitration in New York, New York.

Under the terms of the securities, a holder of any security is deemed to have agreed to the use of arbitration to resolve any dispute, controversy or claim against Brazil arising out of or relating to the securities (other than any action arising out of or based on United States federal or state securities laws) unless such holder elects to bring such claim in an action in Brazil.

The decision of any arbitral tribunal shall be final to the fullest extent permitted by law. Brazil has agreed that any New York court or Brazilian court lawfully entitled to do so may enter a judgment recognizing such an arbitral award. Brazil has agreed that in any arbitration or related legal proceedings for the conversion of an arbitral award into a judgment, it will not raise any defense that it could not raise but for the fact that it is a sovereign state and has consented to the jurisdiction of the United States District Court for the Southern District of New York for the limited purpose of converting into a judgment an arbitral award rendered against Brazil in New York. The realization upon an arbitral award rendered against Brazil would depend upon the application of the United States Foreign Sovereign Immunities Act of 1976, as amended (the "FSIA").

Brazil has not otherwise consented to the jurisdiction of any court outside Brazil in connection with actions arising out of or based on the securities, has not appointed any agent for service of process other than for the purpose of converting an arbitral award into a judgment, and has not agreed to waive any defense of sovereign immunity to which it may be entitled in any action other than in an action to recognize an arbitral award or in an action brought in Brazil. Brazil has agreed that any process or other legal summons in connection with obtaining judicial acceptance of any arbitral award in the United States District Court for the Southern District of New York may be served upon it by delivery to the *Advogado Geral da União* (Attorney General) of Brazil of letters rogatory or by any other means permissible under the laws of the State of New York and Brazil.

Because Brazil has not waived its sovereign immunity in connection with any action brought outside Brazil arising out of or relating to the securities (including without limitation any action arising out of or based on United States federal or state securities law) other than in the limited circumstances described above in connection with an action for the judicial recognition of an arbitral award, it will not be possible to obtain a United States judgment against Brazil unless a court were to determine that (i) Brazil is not entitled under FSIA to sovereign immunity with respect to such actions and (ii) the matter should not be referred to arbitration as contemplated by the securities. Any judgment rendered against Brazil by a court outside Brazil in an action in which Brazil has not submitted to the jurisdiction of such court or otherwise expressly waived its defense of sovereign immunity would not be enforceable against Brazil under its laws.

The enforcement by a Brazilian court of a foreign judgment based upon a foreign arbitral award is subject to the recognition of such judgment by the Federal Supreme Court of Brazil. The Federal Supreme Court will recognize such a judgment if all of the required formalities are observed and the judgment does not contravene Brazilian national sovereignty, public policy and "good morals". Under Article 67 of the Civil Code of Brazil, the public property of the Republic located in Brazil is not subject to execution or attachment, either prior to or after judgment. The execution of a judgment against the Republic in Brazil is only available in accordance with the procedures set forth in Article 730 *et seq.* of the Brazilian Civil Procedure Code, which envisions the registration of the judgment for inclusion in the budget for payment in a subsequent fiscal year of the Republic.

Notwithstanding the foregoing, a holder of any security may institute legal proceedings against Brazil in the federal courts of Brazil, and Brazil has waived any immunity from jurisdiction or execution of judgment in Brazil (except for the limitation on alienation of public property referred to in Article 67 of the Civil Code of Brazil) to which it might otherwise be entitled in any such proceeding.

PLAN OF DISTRIBUTION

Brazil may sell any combination of the debt securities and/or warrants in any of three ways:

- through underwriters or dealers;
- directly to one or more purchasers; or
- through agents.

Each prospectus supplement will set forth:

- the name or names of any underwriters or agents;
- the purchase price of the securities of that series;
- the net proceeds to Brazil from the sale of these securities;
- any underwriting discounts, agent commissions or other items constituting underwriters' or agents' compensation;
- any initial public offering price; and
- any discounts or concessions allowed or reallowed or paid to dealers and any securities exchanges on which the securities may be listed.

The securities may be sold from time to time in distinct series by different means at different prices that are negotiated and fixed or that vary based on market prices.

Underwriters used in the sale of securities will distribute these securities on a firm commitment basis. In this case, the underwriters will acquire these securities for their own account and may resell them from time to time in one or more transactions, including negotiated transactions, at a fixed public offering price or at varying prices to be determined at the time of sale. Brazil may offer the securities to the public either through underwriting syndicates represented by managing underwriters or directly by underwriters. Unless otherwise set forth in the applicable prospectus supplement, the obligations of the underwriters to purchase the securities will be subject to certain conditions precedent and the underwriters will be obligated to purchase all such securities if any are purchased. The underwriters may change any initial public offering price and any discounts or concessions allowed or reallowed or paid to dealers.

Brazil may also sell securities of any series directly to the public or through agents designated by Brazil from time to time. Unless otherwise specified in the applicable prospectus supplement, an agent used in the sale of securities will sell the securities on a reasonable best efforts basis for the period of its appointment.

Brazil may authorize agents, underwriters or dealers to solicit offers by certain specified entities to purchase the securities from Brazil under "delayed delivery" contracts. Purchasers of securities under delayed delivery contracts will pay the public offering price plus accrued interest, if any, and will take delivery of these securities on a date or dates stated in the applicable prospectus supplement. Delayed delivery contracts will be subject only to those conditions set forth in the applicable prospectus supplement. The applicable prospectus supplement will set forth the commission payable for solicitation of these delayed delivery contracts.

Brazil may offer the securities of any series to present holders of other securities of Brazil as consideration for the purchase or exchange by Brazil of other securities. This offer may be in connection with a publicly announced tender, exchange or other offer for these securities or in privately negotiated transactions. This offering may be in addition to or in lieu of sales of securities directly or through underwriters or agents as set forth in the applicable prospectus supplement.

Brazil may agree to indemnify agents and underwriters against certain liabilities, including liabilities under the United States Securities Act of 1933, or to contribute to payments which the agents or underwriters may be required to make in respect of any of these liabilities. Agents and underwriters may engage in transactions with or perform services for Brazil in the ordinary course of business.

VALIDITY OF THE SECURITIES

The validity of the debt securities and warrants will be passed upon for Brazil by Dr. Almir Martins Bastos, *Procurador-Geral da Fazenda Nacional* (Attorney General of the National Treasury), or, in his absence, by a duly authorized attorney of the National Treasury and by Arnold & Porter, United States counsel to Brazil, and for the underwriters, if any, by United States counsel and Brazilian counsel to the underwriters named in the applicable prospectus supplement.

As to all matters of Brazilian law, Arnold & Porter may rely on the opinion of the *Procurador-Geral da Fazenda Nacional.* As to all matters of United States law, the *Procurador-Geral da Fazenda Nacional* may rely on the opinion of Arnold & Porter. Certain statements with respect to matters of Brazilian law in this prospectus have been passed upon by the *Procurador-Geral da Fazenda Nacional,* and are made upon his authority.

OFFICIAL STATEMENTS

Information included in this prospectus which is identified as being derived from a publication of, or supplied by, Brazil or one of its agencies or instrumentalities is included on the authority of that publication as a public official document of Brazil. All other information in this prospectus and the registration statement (of which this prospectus is a part) is included as a public official statement made on the authority of Pedro Sampaio Malan, Minister of Finance.

AUTHORIZED REPRESENTATIVE

The authorized representative of Brazil in the United States of America is Rubens A. Barbosa, the Ambassador of Brazil to the United States of America, whose address is:

Embassy of Brazil
3006 Massachusetts Avenue, N.W.
Washington, D.C. 20008.

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Until the introduction of the *real* in July 1994, Brazil had experienced high rates of inflation. A variety of indices exist for measuring inflation in Brazil. This document uses the General Price Index-Domestic Supply, a national price index based on a weighting of three other indices ("GPI-DS"), the Wholesale Price Index-Domestic Supply ("WPI-DS") (60%), the Consumer Price Index ("CPI") (30%), and the National Index of Building Costs ("NIBC") (10%). The GPI-DS, one of the most widely used inflation indices, is calculated by the Getúlio Vargas Foundation, an independent research organization. See "The Brazilian Economy—Prices". As measured by the GPI-DS, the annual rate of inflation in Brazil was 1.7% in 1998, 7.5% in 1997, 9.3% in 1996, 14.8% in 1995, but was 909.6% for 1994 and 2,708.6% for 1993. Other inflation indices from time to time show higher inflation rates than the GPI-DS. Such high historical levels of inflation, together with the devaluation of the Brazilian currency in relation to the U.S. dollar, render comparisons of year-to-year financial performance and U.S. dollar translations less meaningful. Accordingly, the effects of inflationary distortions should be considered by the readers of all financial and statistical information contained herein. Except as indicated herein, the exchange rates used herein to convert pre-Cruzado Plan *cruzeiro, cruzado, cruzado novo,* post-Cruzado Plan *cruzeiro, cruzeiro real or real* amounts into U.S. dollars for a particular period were the commercial rates of exchange recorded by the Central Bank in effect at the end of such period. These conversions are provided solely for the convenience of readers of this document and should not be construed as implying that the Brazilian currency amounts represent or have been or could be converted into U.S. dollars at such rates.

The following table sets forth certain exchange rate information for the selling of U.S. dollars, expressed in nominal *reais,* for the periods indicated. The Federal Reserve Bank of New York does not report a noon buying rate for the *real* and did not report a noon buying rate for its predecessor currency, the *cruzeiro real.*

Table No. 1

Commercial Exchange Rates (Selling Side)
R$/$(1)

Year	Average for Period(2)	End of Period	Percentage Change (End of Period)
1994	0.6450	0.8460	613.4
1995	0.9177	0.9725	15.0
1996	1.0052	1.0394	6.9
1997	1.0787	1.1164	7.4
1998	1.161[illegible]	1.2087	8.3

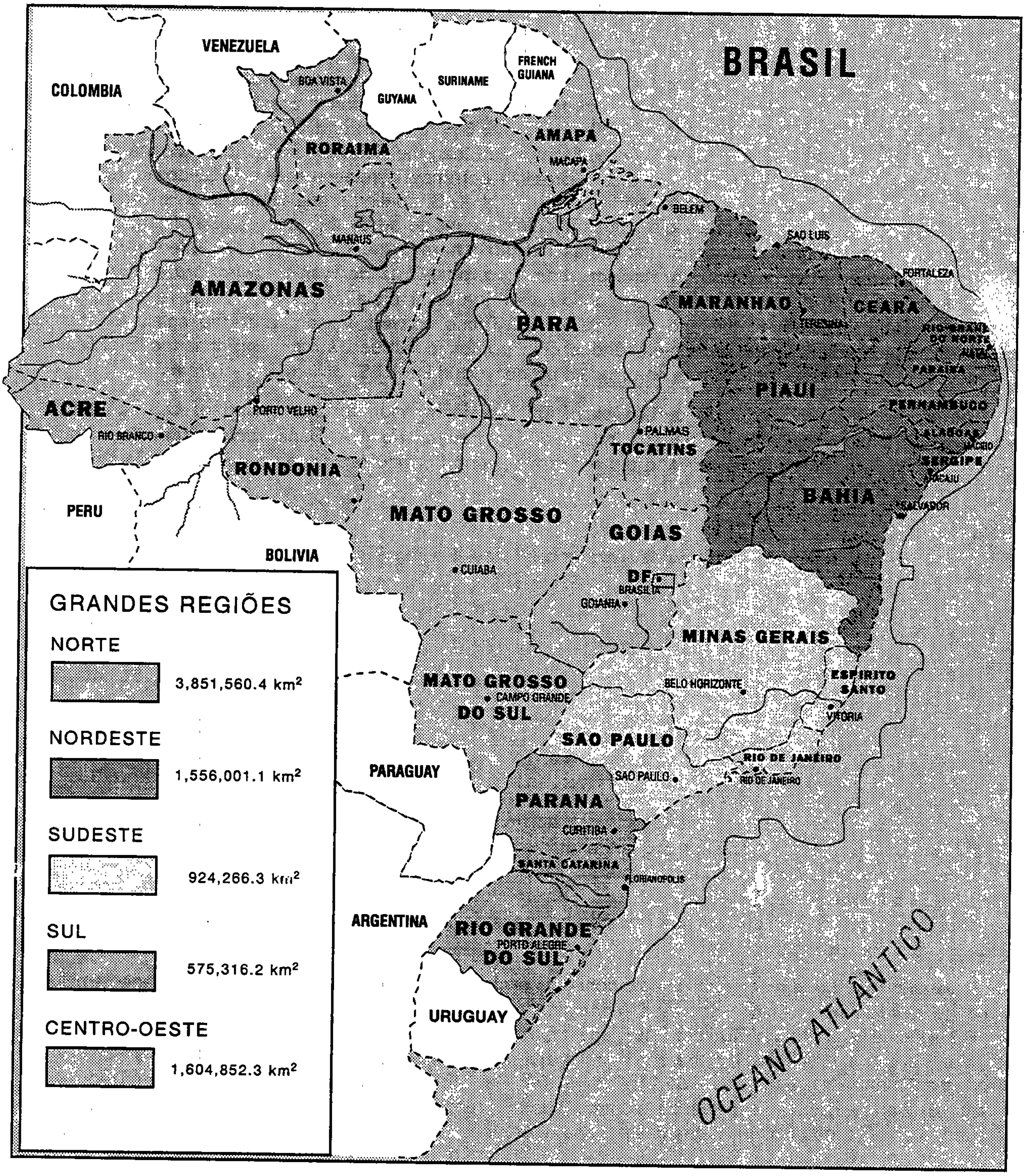
(1) Amounts expressed in *reais* have been translated from the predecessor currencies in effect during the relevant period, at the rates of exchange at the time the successor currency became the lawful currency of Brazil. Accordingly, *cruzeiros reais* have been translated into *reais* at the rate of CR$2,750.00 to R$1.00.

(2) Weighted average of the exchange rates on business days during the period.

Source: Central Bank

In January 1999, the Central Bank abandoned its exchange band mechanism, which encouraged small exchange devaluations within a specified range and which had been in effect since March 1995, and permitted the value of the *real* to float freely against that of the dollar. On August 31, 1999, the *real*-U.S. dollar exchange rate (sell side) in the commercial exchange market, as published by the Central Bank of Brazil (the "Central Bank"), was R$1.9159 to $1.00. See "Balance of Payments and Foreign Trade—Foreign Exchange Rates and Exchange Controls". In this report, references to "dollars", "U.S. dollars", "$" and "U.S.$" are to United States dollars, and references to "*real*", "*reais*" and "R$" are to Brazilian *reais.*

The fiscal year of the federal Government of Brazil (the "Government") ends December 31. The fiscal year ended December 31, 1998 is referred to in this Prospectus as "1998", and other years are referred to in a similar manner. Tables herein may not add due to rounding.


BRASIL
VENEZUELA
COLOMBIA
GUYANA
SURINAME
FRENCH GUIANA
BOA VISTA
RORAIMA
AMAPA
MACAPA
BELEM
SAO LUIS
FORTALEZA
MANAUS
AMAZONAS
PARA
MARANHAO
CEARA
TERESINA
RIO GRANDE DO NORTE
PARAIBA
PIAUI
PERNAMBUCO
ALAGOAS
SERGIPE
ACRE
PORTO VELHO
RIO BRANCO
PALMAS
TOCATINS
RONDONIA
BAHIA
SALVADOR
PERU
MATO GROSSO
GOIAS
BOLIVIA
CUIABA
DF
BRASILIA
GOIANIA
MINAS GERAIS
ESPIRITO SANTO
VITORIA
BELO HORIZONTE
MATO GROSSO DO SUL
CAMPO GRANDE
SAO PAULO
RIO DE JANEIRO
PARAGUAY
PARANA
CURITIBA
SANTA CATARINA
FLORIANOPOLIS
ARGENTINA
RIO GRANDE DO SUL
PORTO ALEGRE
URUGUAY
OCEANO ATLANTICO
GRANDES REGIÕES
NORTE
3,851,560.4 km²
NORDESTE
1,556,001.1 km²
SUDESTE
924,266.3 km²
SUL
575,316.2 km²
CENTRO-OESTE
1,604,852.3 km²

INTRODUCTION

General. Brazil is the fifth largest country in the world and occupies nearly half the land area of South America. Brazil shares a border with every country in South America except Chile and Ecuador. The capital of Brazil is Brasília, and the official language is Portuguese. At December 31, 1998, Brazil's estimated population was 161.8 million, the fifth largest in the world.

Following two decades of military governments, in 1985 Brazil made a successful transition to civilian authority and democratic government. A new Brazilian Constitution (the "Constitution") was promulgated in 1988. In 1989, direct presidential elections were held for the first time in 29 years. The second such election occurred on October 3, 1994, at which time Fernando Henrique Cardoso, Minister of Finance from April 1993 to April 1994 and the primary advocate of the *Plano Real*, was elected President. Mr. Cardoso assumed office on January 1, 1995 for a term of four years. In connection with the continuation of the *Plano Real*, the Cardoso administration has advocated a number of constitutional amendments and other measures designed to effect fundamental changes in Brazil's public finances. These include, among others, reforms of the tax and social security systems, modification of the scope of certain state monopolies, changes in the spending responsibilities of different levels of government and changes in conditions of employment in the public sector. The Cardoso administration has also taken steps to further Brazil's economic liberalization process and has pursued the passage of a number of constitutional amendments and legislative measures designed to further deregulate the Brazilian economy, reduce the Government's fiscal deficit and encourage foreign capital investment. Mr. Cardoso was reelected to a second term of office as President of Brazil in national elections that occurred on October 5, 1998. Mr. Cardoso's second four-year term of office began on January 1, 1999.

The *Plano Real,* which the Government announced in December 1993, succeeded in lowering inflation from an annual rate of 2,708.6% in 1993 and 909.6% in 1994 to 14.8% in 1995, 9.3% in 1996, 7.5% in 1997 and 1.7% in 1998, as measured by the GPI-DS. Cumulative inflation, as measured by GPI-DS for the period from July 1, 1994 through December 31, 1998, totalled 60.5%. Meanwhile, real gross domestic product ("GDP") rose 5.9% in 1994, 4.2% in 1995, 2.7% in 1996 and 3.2% in 1997 but declined 0.1% in 1998. The inflation rate has risen in 1999, however, following the decision of the Central Bank in January 1999 to permit the value of the *real* to float against that of the dollar. See "The Brazilian Economy—*Plano Real* and Current Economic Policy" and "Balance of Payments and Foreign Trade—Foreign Exchange Rates and Exchange Controls". The inflation rate registered 12.6% for the twelve months ended August 31, 1999. The Cardoso administration has sought to build upon the initial success of the *Plano Real* by advocating broader measures to address what it regards as underlying structural problems that have distorted fiscal and monetary policy. Prior to the introduction of the *real* as Brazil's official currency in July 1994 pursuant to the *Plano Real*, Brazil's economic performance had been characterized by macroeconomic instability, including extremely high rates of inflation and significant and sudden currency devaluations. See "The Brazilian Economy—Recent Performance", "—*Plano Real* and Current Economic Policy" and "—Prices". Pre-*Plano Real* stabilization efforts, which included wage and price controls, failed to contain inflation for any extended period.

The continued success of the *Plano Real* depends on the ability of the Government to maintain fiscal restraint and a tight monetary policy in the face of both domestic and international economic pressures as well as, in the long term, on the ability of the Government to implement structural reforms, such as reform of the tax and social security systems, transfer of certain federal spending responsibilities to State governments and privatization of major enterprises, some of which reforms require either additional constitutional amendments or implementing legislation. Whereas amendments to the Constitution require three-fifths of the votes of the respective members of each house of Congress in two separate rounds, ordinary legislation requires only a simple majority of both houses of Congress. President Cardoso's party, which holds the third largest block of seats in Congress, does not alone have sufficient votes to ensure passage of such amendments or related implementing legislation, and proposed amendments have been modified after negotiations with Congress in order to secure their passage. Consequently, the ability of the Cardoso Government to effect lasting economic reforms depends upon a shifting coalition that includes a variety of political parties with varying degrees of stated commitment to these measures. See "The Federative Republic of Brazil—Form of Government and Political Parties".

Reduced inflation in Brazil has had a significant effect on the country's banking system, resulting in the decline of sources of profit associated largely with high inflation (such as spread or "float" revenue earned through financial intermediation). Following the introduction of the *Plano Real,* the Central Bank assumed administrative control of several large financial institutions, including Banco do Estado de São Paulo S.A. ("BANESPA") and Banco do Estado do Rio de Janeiro S.A. ("BANERJ"), banks owned by the States of São Paulo and Rio de Janeiro, respectively, as well as major private sector banks such as Banco Econômico S.A., and helped arrange the restructuring and sale of significant assets of others, including Banco Nacional S.A. and Banco Bamerindus S.A. From the introduction of its Program of Incentives for Restructuring and Strengthening of the National Financial System (PROER) in November 1995 through December 31, 1998, the Central Bank made gross disbursements thereunder of approximately R$21.0 billion, primarily for the restructuring of Banco Nacional S.A., Banco Econômico S.A. and Banco Bamerindus S.A.; this amount does not reflect any assistance that may eventually be provided to other banks which may become eligible for assistance in the future. See "The Financial System—General". The Government in 1996 increased by R$8 billion the capital of Banco do Brasil S.A. ("Banco do Brasil"), a Government-controlled bank and Brazil's largest commercial bank, which reported a 1995 loss in excess of R$4 billion and a 1996 loss of R$7.5 billion. This capital increase was funded by issuance of National Treasury Notes (R$6.5 billion) and by investments made in Banco do Brasil by the Banco do Brasil Employee Pension Fund ("PREVI") (R$1 billion) and the National Bank for Economic and Social Development Holdings ("BNDESpar") (R$500 million), a subsidiary of the National Bank for Economic and Social Development ("BNDES"). In addition, on February 28, 1997, the Government established the Support Program for the Reduction of the State Public Sector in Banking Activity (PROES) to facilitate the privatization or other disposition of Brazilian State-owned banks. As of December 31, 1998, 40 State financial institutions had sought PROES assistance, with a majority electing to be privatized or converted into a development agency. See "The Financial System—General". In late October 1997, following a sell-off of Brazilian securities and related declines in the Brazilian stock markets, the Central Bank advanced amounts to certain financial institutions through its discount window. Such amounts were intended to address such institution's short-term liquidity requirements. As of November 10, 1997, all such advances had been repaid. The average daily balance of outstanding advances made through the Central Bank's discount window between November 10, 1997 and November 25, 1997 was approximately R$1.1 billion.

Foreign trade and foreign investment have contributed to Brazil's economic development. Brazil's overall trade flows have grown markedly in recent years, rising from $63.8 billion in 1993 to $112.8 billion in 1997, a 76.8% increase. Much of the increase was attributable to the rise in imports; imports rose from $25.3 billion in 1993 to $59.8 billion in 1997, a 136.9% increase. During the same period, exports grew by 37.4%, from $38.6 billion in 1993 to $53.0 billion in 1997. As a result, the trade balance moved from a surplus of $13.3 billion in 1993 to a deficit of $6.8 billion in 1997. Because of the decline in economic activity in 1998, Brazil's overall trade flows declined to $108.8 billion that year. Imports declined by 3.5% to $57.7 billion in 1998, while exports declined by 3.5% to $51.1 billion. Brazil ended the year with a trade deficit of $6.6 billion. The current account recorded deficits in each of the five years ended December 31, 1998 due to increased expenditures on services and a deteriorating trade balance. At December 31, 1998, Brazil's current account deficit reached $34.3 billion. Brazil's capital account, however, recorded a surplus during those years as a result of net capital inflows and, in 1994, the restructuring of the Republic's external indebtedness. Notwithstanding the surplus in its capital account, the balance of payments registered deficits of $7.9 billion in 1997 and $17.3 billion in 1998, after having recorded surpluses in the previous four years. Brazil's trade deficit for the first eight months of 1999 totalled $0.7 billion. See "Balance of Payments and Foreign Trade—Foreign Trade" and "—Balance of Payments".

As of December 31, 1995, foreign direct investment (excluding intercompany loans) from a large number of countries, as registered with the Central Bank, totalled approximately $42.7 billion. Mainly as a result of increases in foreign investment in 1995, Brazil's international reserves increased from $38.8 billion at December 31, 1994 to $51.8 billion at December 31, 1995, notwithstanding the decline of foreign investment in Brazil during the first quarter of 1995, due in part to the effects of the Mexican liquidity crisis and concerns about a potential devaluation of the *real*. Investors' liquidity needs and concerns about potential currency devaluation led to a net outflow of $3.7 billion of portfolio investments in the first quarter of 1995. This situation was reversed in the second, third and fourth quarters of 1995, with net inflows of $3.7 billion, $7.1 billion and $3.0 billion, respectively, in portfolio investments. Total net inflows of foreign investments in 1995 reached $14.3 billion, a 5.7% increase over the $13.5 billion recorded in 1994. Total net inflows more than doubled in 1996, amounting to $31.7 billion. Net foreign portfolio investment inflows reached $21.8 billion in 1996, a 117.9% increase over the amount of such inflows in 1995, and net direct investment inflows totalled $9.9 billion (excluding intercompany loans) in 1996, a 129.3% increase from the previous year. See "Balance of Payments and Foreign Trade—General" and "—Foreign Investment". Largely as a result of such inflows, Brazil's international reserves rose to $60.1 billion at December 31, 1996, a 16.0% increase over the $51.8 billion recorded at December 31, 1995, notwithstanding Brazil's $5.6 billion trade deficit in 1996.

The Asian financial crisis and the ripple effects of that crisis have presented a continuing challenge for Brazil. The Government used a portion of its international reserves to intervene in the foreign exchange markets following a sell-off of Brazilian securities in late October 1997 and related declines in the Brazilian stock markets, causing international reserves to fall to approximately $52.2 billion at December 31, 1997. In addition, the Central Bank took temporary measures designed to provide long-term stability in the Brazilian capital markets and to moderate surges in capital outflows. See "The Brazilian Economy—*Plano Real* and Current Economic Policy". The sell-off of Brazilian securities and related declines in the Brazilian stock markets had an adverse effect on foreign investment flows to Brazil in 1997. Brazil ended the year with total net foreign investment of $26.2 billion, a 17.5% decline from 1996, with net foreign portfolio investment down 58.1% to $9.1 billion. However, net foreign direct investment reached $17.1 billion in 1997, a 71.3% increase over 1996.

Brazil's international reserves recovered during the first four months of 1998, reaching a historical high of $74.7 billion at April 30, 1998. At July 31, 1998, Brazil's international reserves stood at approximately $70.2 billion, corresponding to approximately 14 months of imports. In the ensuing months, however, international reserves came under pressure. The Government believes that the pressure was, in part, the result of investors' decisions to reduce their exposure to emerging markets after expectations regarding emerging markets, in general, changed based on adverse developments in Russia. Although outflows in August 1998 were partially offset by net foreign direct investment, primarily resulting from the privatization of Telecomunicações Brasileiras S.A. ("Telebrás"), Brazil's international reserves declined to $67.3 billion at August 31, 1998, $45.8 billion at September 30, 1998 and $42.4 billion at October 31, 1998.

In response to this outflow of international reserves, the Government, among other things, (i) raised the Central Bank's assistance rate (TBAN) to 49.75% from 29.75% per annum, (ii) temporarily eliminated financial institutions' access to funds at the Central Bank's basic rate (TBC), (iii) reduced the minimum term for new foreign currency debt to one year from two years and (iv) reduced the minimum term for the rollover of foreign currency debt to six months from one year. In addition, on October 28, 1998, the Government announced a set of measures, collectively referred to as the Fiscal Stabilization Program, that are intended to produce a primary surplus of 2.6% of GDP in 1999, 2.8% of GDP in 2000 and 3.0% GDP in 2001. The Fiscal Stabilization Program had two components: (1) structural measures to address the roots of fiscal disequilibrium and (2) the Action Plan for 1999-2001. The structural measures included:

(a) the implementation of the measures included in the Constitutional Amendment No. 19 relating to administrative reform (see "The Brazilian Economy—Constitutional Reform");

(b) the proposal and enactment of a fiscal responsibility law that, among other things, established ceilings on public expenditure and indebtedness for all three levels of government and imposed sanctions for noncompliance;

(c) the simplification of the tax system through, among other things, a reduction in the number of taxes collected; and

(d) the reform of the budgetary process.

The Action Plan for 1999-2001 included, among other things,

(i) spending cuts for state enterprises for 1999 of approximately R$2.7 billion,

(ii) extending to retired civil servants the obligation to make social security contributions in an amount equal to 11% of their pensions,

(iii) imposing a 9% supplemental social security contribution on persons earning salaries or receiving pensions over R$1,200 per month for a period of five years,

(iv) extending the provisional financial contribution transaction levy (CPMF), which was due to expire on December 31, 1998, and increasing that tax from the current rate of 0.20% to 0.38% in 1999 and 0.30% in 2000 and 2001,

(v) increasing the contribution for social purposes (COFINS) by one percentage point (to 3% from 2%) and extending the application of that tax to the financial sector, which had previously been exempt, and

(vi) extending the term of the Fiscal Stabilization Fund (FEF) to 2006 and increasing the amount retained by the Government from the present 20% of certain tax revenues to 40% of such tax revenues in 2000 to 2006.

See "The Brazilian Economy—Constitutional Reform—Provisional Financial Contribution Transaction Levy" and "Public Finance –Taxation and Revenue Sharing Systems". The Go ernment estimates for the Fiscal Stabilization Program assumed reduced GDP growth of 0.5% in 1998 and negative 1.0% in 1999. GDP declined 0.1% in 1999.

The Government made some initial progress in implementing the Fiscal Stabilization Program and Action Plan. On November 18, 1998, the National Congress approved four fiscal measures, including the proposed extension to retirees of the obligation to make social security contributions, the proposed increase to 3% of the COFINS rate and the extension of that tax to the financial sector, which previously had been exempt. On November 26, 1998, the Government delivered to the National Congress legislation to simplify the tax system by, among other things, eliminating six existing taxes (including COFINS, the federal tax on industrial products (IPI) and the state tax on the circulation of goods and services (ICMS) and replacing them with a single value-added tax. The bill also proposed to introduce a permanent federal tax on financial transfers (IMF) to replace the provisional financial contribution levy (CPMF).

In addition, on November 13, 1998, the International Monetary Fund (IMF) announced a $41.8 billion support package for Brazil, approximately $18.3 billion of which is to be provided by the IMF and $4.5 billion by each of the World Bank and the Inter-American Development Bank. An additional $14.5 billion is to be provided by 20 countries through a credit facility coordinated by the Bank for International Settlements and the Ministry of Finance of Japan. Of the support package resources, $32.2 billion would be available to Brazil during the first 12 months, if needed. Brazil received the first installment of approximately $9.3 billion in two disbursements, following the approval of the IMF's component of the support package by its Executive Board on December 3, 1998 and the ratification of the package by the Brazilian Senate.

Brazil's international reserves stabilized following the announcement of the support package, reaching $41.2 billion at November 30, 1998. The Central Bank also lowered the TBAN rate during this time from 49.75% to 42.25% on November 12, 1998 and 36% on December 17, 1998. In December 1998, however, there were significant outflows following the Government's failure to secure passage of a key social security reform bill by the Chamber of Deputies in a December 3, 1998 vote and delays in the voting of the increase of the CPMF rate. After giving effect to such outflows and the $9.3 billion inflow from the IMF-led support package, reserves stood at $44.6 billion at December 31, 1998. On December 31, 1998, the *real*-U.S. dollar exchange rate (sell side) in the commercial exchange market, as published by the Central Bank, stood at R$1.2087 to $1.00.

In January 1999, Brazil's international reserves came under significant pressure once again as a result of a series of events that month. On January 6, 1999, the newly inaugurated governor of the State of Minas Gerais announced that the State would suspend for 90 days payments in respect of the State's approximately R$18.3 billion debt to the Government. A week later, on January 13, 1999, Gustavo H.B. Franco, the president of the Central Bank and one of the architects of the *Plano Real,* resigned and was replaced by Francisco Lopes, who attempted a controlled devaluation of the *real* by widening the band within which the *real* was permitted to trade. Subsequent Central Bank intervention failed to keep the *real*-U.S. dollar exchange rate within the new band, however, and on January 15, 1999, the Central Bank announced that the *real* would be permitted to float, with Central Bank intervention to be made only in times of extreme volatility. Following that announcement, the value of the *real* against the U.S. dollar declined approximately 21% from its level on January 12, 1999.

To minimize excessive exchange rate volatility and reduce the inflationary effects of the devaluation of the *real,* the Central Bank raised its assistance rate (TBAN) to 41% from 36% on January 19, 1999, and the Central Bank intervened in the market to adjust the Federal Funds Rate (*taxa Over/Selic*) to 32% on January 19, 1999 from 29.8% the previous day. The *Over/Selic* rate was further increased to 35.5% on January 28, 1999 and 37.0% on January 29, 1999. Both the level of international reserves and the value of the *real* continued to decline, however; as of January 31, 1999, Brazil's international reserves stood at $36.1 billion, and the *real*-U.S. dollar exchange rate (sell side) in the commercial exchange market, as published by the Central Bank, stood at R$1.9832 to $1.00.

In the weeks following the decision to permit the *real* to float, the Government continued its efforts to implement the expense reduction and revenue enhancement measures under its Fiscal Stabilization Program. On January 20, 1999, the Chamber of Deputies, reversing its December 3, 1998 vote, approved legislation to extend to retired civil servants the obligation to make social security contributions in respect to their monthly pensions at tax rates ranging from 11% to 25% of the amount of their monthly pensions in excess of R$600. The bill also increased the social security contribution of active civil servants earning more than R$1,200 per month. This legislation, which was approved by the Senate on January 26, 1999, became law on January 28, 1999. The Congress also approved an austerity budget on January 25, 1999 that provided for spending cuts of approximately R$8.7 billion. In addition, the Chamber of Deputies approved on March 18, 1999, in the second round of voting, a bill that would increase the provisional financial contribution transaction levy (CPMF) to 0.38% from 0.20%. This measure had previously been approved by the Senate. The increased CPMF tax will be collected during the second half of 1999.

On February 2, 1999, when the cumulative devaluation (since January 13, 1999) of the *real* against the U.S. dollar exceeded 40%, the Government designated Armínio Fraga Neto to replace Francisco Lopes as president of the Central Bank. Following Mr. Fraga's confirmation on March 3, 1999, the Central Bank eliminated the TBC and TBAN rates, giving primacy to the *Over/Selic* rate; because the Central Bank can influence the *Over/Selic* rate on a daily basis through its participation in auctions, repurchase transactions and reverse repurchase transactions, the *Over/Selic* rate permits the Central Bank to react more quickly to changes in market conditions. The Central Bank also increased the *Over/Selic* rate to 45% from 39%. The Central Bank subsequently reduced the *Over/Selic* rate to 42% on March 25, 1999, 39.5% on April 6, 1999, 34% on April 15, 1999, 32% on April 29, 1999, 29.5% on May 10, 1999, 27%

on May 13, 1999, 23.5% on May 20, 1999, 22% on June 9, 1999 and 21% on June 24, 1999, citing lower-than-expected inflation and improved expectations for the economy. The *Over/Selic* rate was further reduced to 19.5% on July 28, 1999 and 19% on September 22, 1999.

Brazil also began negotiations with the IMF on adjustments to the 1999-2001 economic program agreed in November 1998 and new economic targets in light of the new foreign exchange regime introduced in January 1999 and, on March 5, 1999, Brazil and the IMF announced that they had reached agreement. Under the agreement, Brazil has undertaken to adopt measures designed to achieve primary surpluses, excluding debt payments, of at least 3.1% of GDP in 1999, 3.25% of GDP in 2000 and 3.35% of GDP in 2001, substantially greater than the 2.6%, 2.8% and 3.0% of GDP surpluses for 1999, 2000, and 2001, respectively, under the November 13, 1998 agreement with the IMF. The public debt/GDP ratio, currently in excess of 50%, is also targeted to fall below 46.5% at year-end 2001. The Memorandum of Economic Policy annexed to the IMF letter of intent noted that certain of the measures intended to produce the agreed-upon primary surpluses had already been approved or announced, including (i) the suspension until the end of 1999 of PIS/COFINS credits for exports, (ii) an increase in the IOF for consumer lending and (iii) the submission to the Congress of legislation to require military personnel to make contributions to the social security system. Brazil has also agreed to reduce the investment budgets of state-owned companies by 0.9% of GDP, accelerate the privatization of state enterprises and promote the independence of the Central Bank through, among other things, the introduction of fixed terms for the president and directors of the Central Bank. The new agreement anticipated a decline in GDP of approximately 3.5% to 4.0% for 1999, while inflation was expected to increase initially above a 10% per annum rate in the first part of 1999, decreasing gradually during the second half to result in an average monthly inflation rate of 0.5% to 0.7% at year-end 1999. Under the revised program, the trade deficit, which had been projected to be $6.4 billion for 1999, was expected to revert to a surplus of approximately $11.0 billion, and the current account deficit was targeted to fall from 4.5% of GDP to 3.0% of GDP.

On April 6, 1999, Brazil received a second disbursement, of approximately $4.9 billion, from the IMF, which was followed by an additional $4.9 billion in bilateral loans on April 9, 1999 under the IMF-led support package. Subsequent disbursements under the IMF's letter of intent will be based on Brazil's ability to meet the primary surplus targets described above and on the Republic's progress in implementing the promised fiscal reforms. There can be no assurance that Brazil will be able to meet the primary surplus targets under its agreement with the IMF and, accordingly, that the full amount under the IMF-led support package will be available to Brazil. See "Public Debt—Debt Crisis and Restructuring".

After giving effect to the inflows from the IMF-led support package and an offering of debt securities by the Republic in April 1999 (see "Public Debt—Debt Crisis and Restructuring"), Brazil's international reserves stood at $44.3 billion on April 30, 1999, up from $35.5 billion at February 28, 1999 and $33.8 billion at March 31, 1999. The *real*-U.S. dollar exchange rate (sell side) in the commercial exchange market on April 30, 1999, as published by the Central Bank, stood at R$1.6607 to $1.00, up from R$1.722 to $1.00 on March 31, 1999, and the average *real*-U.S. dollar exchange rate during January 1999 and February 1999 was R$1.5019 to $1.00 and R$1.9137 to $1.00, respectively, versus R$1.2106 to $1.00 immediately prior to the widening of the trading band.

Despite the foregoing events, total net foreign investment increased 69.4% in 1998 to $44.4 billion. Net portfolio investment more than doubled in 1998 to $18.2 billion, but was still lower than the $21.8 billion recorded in 1996. Foreign direct investment inflows increased 53.0% in 1998, totaling $26.1 billion. Of that amount, 23.4%, or $6.1 billion, resulted from foreign participation in the national privatization program. In the first eight months of 1999, foreign direct investment inflows totalled $19.9 billion, bringing such investment to $30.6 billion in the twelve months ended August 31, 1999.

On June 18, 1999, the Government repaid approximately 30% of the initial disbursement by the Bank for International Settlements and the Ministry of Finance of Japan under the $41.8 billion IMF-led support plan, together with approximately $221.8 million in interest. The remaining 70% was rolled over for another six months.

On July 5, 1999, the Government released the Memorandum of Economic Policy resulting from the IMF's third review of Brazil's performance under the IMF-led support program established in December 1998. The Memorandum reported that the Brazilian economy was performing better than originally forecast. According to the Memorandum, GDP growth fell less rapidly than predicted during the first quarter of 1999, reflecting significant increases in agricultural production; GDP was expected to decline by approximately 1% or less in 1999, versus the 3.5% to 4.0% decline forecast in the March 8, 1999 Memorandum of Economic Policy. In addition, the inflation rate (as measured by IGP-DS) during the first five months of 1999 was 7.4%, versus the 11% rate that had been previously forecast. However, the trade balance continued to show a slight deficit during the first five months of 1999, and the surplus was therefore likely to be lower than projected (approximately $4.0 billion versus the $10.8 billion previously forecast).

The Memorandum left unchanged the primary surplus targets described in the March 8, 1999 Memorandum of Economic Policy but includes inflation targets of 8% in 1999, 6% in 2000 and 4% in 2001, as measured by the IBGE's IPCA index. The Government has also undertaken to continue its efforts to implement fiscal and structural reforms intended to meet the targets under the March 8, 1999 Memorandum of Economic Policy. According to the Memorandum, the Government intends to seek Congressional approval of the Law of Fiscal Responsibility (which would, among other things, establish ceilings on public expenditure and indebtedness for all three levels of government and impose sanctions for noncompliance) and tax reforms, implement legislation recently approved by Congress that is intended to reduce personnel expenses at all levels of government and work with the Congress to develop new measures to shore up the nation's social security system.

As of the date of this document, international financial markets had not yet stabilized, and it is not possible to determine what effect, if any, any continuing instability in such markets would have on the Brazilian economy.

Since 1994, debt management policy has aimed at lengthening the maturity of domestic public debt, as well as consolidating a domestic yield curve by means of selling fixed income government securities. The average maturity of debt was 149 days in December 1989, a period of high inflation, 430 days in September 1997, and 463 days in July 1998. In December 1989, 99% of the debt was indexed (floating-rate securities), compared to 42% in September 1997, and 78% in July 1998. Non-residents holding of government securities is extremely low—approximately 1% of total outstanding domestic debt. The effort to consolidate the domestic yield curve through longer average maturities was temporarily interrupted by the Asian financial crisis in 1997 and the Russian financial crisis in 1998. Upon the return of normal market conditions, it is a major objective of the Government to proceed in the direction that was initiated with the launch of the Real Plan in July 1994.

Unemployment rates declined during the second half of 1998 from 8.02% in July 1998 to 6.32% in December 1998. After rising to 7.73% in January 1999, unemployment rates declined to 7.54%in July 1999, compared with an unemployment rate of 8.02% in July 1998. A large part of the rise in unemployment was attributable to a decline in the level of economic activity. The Fiscal Stabilization Program includes measures to reduce the impact of rising unemployment, such as increased benefits for the long-term unemployed, greater flexibility in work contracts and initiatives to create job opportunities for young citizens. However, the Government expects GDP to decline by 1% in 1999, which may result in further increases in the unemployment rate.

The ability of the Brazilian Government to achieve economic growth targets depends in part on containing public expenditures in order to reduce the public sector borrowing requirement and avoid "crowding out" private sector investment. Expressed as a percentage of GDP, the consolidated operational deficit for the Brazilian public sector reached 4.8% of GDP for 1995, of which the federal

Government, State and local governments and public sector enterprises accounted for 1.7%, 2.3%, and 0.8%, respectively. Such deficits increase the size of the public sector debt and have the effect of reducing total savings available for investment and development in the private sector. In 1996, the consolidated operational deficit was reduced to 3.8% of GDP. Among the measures that contributed to the reduction of the deficit were the following: (i) the approval of the *Fundo de Estabilização Fiscal* (the "Fiscal Stabilization Fund", or "FEF"), (ii) not indexing increases in the minimum wage or in public sector wages to past inflation, (iii) the significant reduction in the Federal Funds Rate (*taxa Over/Selic*) from an average of 53.09% in 1995 to 27.41% in 1996, thereby reducing the cost of servicing public debt, and (iv) the adoption of the Support Program for the Restructuring and Fiscal Adjustment of the States, designed to monitor State and local government spending. See "The Brazilian Economy—*Plano Real* and Current Economic Policy", "—Salaries and Wages", "—Constitutional Reform", "—Changes in the Relationship between the Federal and Local Governments" and "Public Finance—Consolidated Public Sector Fiscal Performance". The consolidated operational deficit rose to 4.3% of GDP in 1997, however, of which 1.7%, 2.3% and 0.3% were attributable to the federal Government, State and local governments and public sector enterprises, respectively. The consolidated operational deficit continued its rise in 1998, reaching 7.5% of GDP, of which the 5.2%, 1.8% and 0.5% were attributable to the federal Government, State and local governments and public sector enterprises, respectively. A proposed constitutional amendment to extend the FEF, which expired on June 30, 1997, was adopted on November 25, 1997 as Constitutional Amendment No. 17 with retroactive effect to June 30, 1997. The FEF is scheduled to expire on December 31, 1999.

Net public sector debt in Brazil, composed of the internal and external debt of the federal Government, State and local governments and public sector enterprises, amounted to approximately $181.5 billion as of December 31, 1994, or 28.1% of GDP. Net public sector debt rose to $214.6 billion at December 31, 1995, or 29.9% of GDP, largely due to the increase in net internal indebtedness to $175.3 billion from $128.9 billion at the end of 1994, as a result of the issuance by the federal Government of domestic debt securities in an effort to absorb excess liquidity in the domestic market. Net public sector debt continued to rise in 1996, 1997 and 1998, totaling $259.2 billion, or 34.4% of GDP, at December 31, 1996, $276.6 billion, or 34.5% of GDP, at December 31, 1997 and $321.8 billion, or 42.6% of GDP, at December 31, 1998. The real average rate of interest on such domestic securities was 23.0% in the twelve-month period ended August 31, 1998 as compared to 33.4% in the twelve-month period ended December 31, 1995. Following the debt- and debt service-reduction agreements implemented on April 15, 1994, the maturity profile of Brazil's public sector external debt was substantially lengthened from an average of 6.9 years at December 31, 1993 to an average of 8.8 years at December 31, 1996. The average maturity of Brazil's public-sector external debt was 7.7 years at December 31, 1997 and 6.9 years at December 31, 1998. Net external public sector debt as a percentage of GDP declined from 8.1% in 1994 to 4.3% as of December 31, 1997 before rising again to 6.6% as of December 31, 1998. Total gross public sector debt as a percentage of GDP increased from 41.4% in 1994 to 59.6% of GDP as of December 31, 1998. As of December 31, 1998, total gross public sector debt was $450.1 billion or 59.6% of GDP. See "Public Debt".

On January 6, 1999, the newly inaugurated governor of the State of Minas Gerais announced that the State would suspend for 90 days payments on its approximately R$18.3 billion debt to the Government. The governor of the State of Rio Grande do Sul subsequently sought and obtained an injunction permitting that State to make payments into an escrow account, pending the resolution of the request of seven States to renegotiate refinancing agreements reached with the Government under Law No. 9,496 of September 11, 1997. See "The Brazilian Economy—Changes in the Relationship between the Federal and Local Governments". The Government responded by withholding Constitutionally mandated transfers payable to the State of Minas Gerais and, on February 10, 1999, paid approximately half of an approximately $85 million due in respect of the State's Eurobonds that matured on that date to ease investor concerns about the risk of default by State governments. The Government also notified certain international financial institutions that it would no longer guarantee these States' obligations to these financial institutions, leading the World Bank to suspend loans to the States of Minas Gerais and Rio Grande do Sul.

In a meeting with the President on February 26, 1999, certain of the governors pressed for a renegotiation of the refinancing agreements. The President offered instead to make loans to the States to cover the costs of layoffs and pension reform and promised to review a law exempting exports from State taxes. The Government has initiated negotiations with the World Bank to secure funding for such loans.

On June 2, 1999, the Central Bank declared the State of Pernambuco in default after the State announced that it would not honor approximately R$260 million aggregate principal amount of the State's bonds. As a result of the default, the State is precluded from borrowing in the local markets.

On April 14, 1999, a Parliamentary Committee of Inquiry (CPI) of the Senate was formed to investigate certain events involving the financial system, including, among other things, allegations that had appeared in the Brazilian press that certain Brazilian and foreign banks had benefited improperly from inside information received prior to the devaluation of the *real* and allegations that had appeared in the Brazilian press that the Central Bank improperly had sold dollars to two Brazilian banks at rates below the prevailing trading price. The Central Bank has delivered to the Senate a detailed report responding to the issues that the Senate has raised. The investigation is continuing.

During the period from 1982 until the implementation of Brazil's external debt restructuring in 1994, Brazil failed to make payments on certain of its external indebtedness from commercial banks as originally scheduled, and in February 1987 declared a moratorium on principal and interest payments on external indebtedness to commercial banks. Brazil's external indebtedness to commercial banks was restructured in a Brady Plan-type restructuring in April 1994. In April 1999, the Republic completed an exchange offer pursuant to which the Republic acquired and cancelled approximately $993.1 million aggregate outstanding principal amount of bonds issued in that restructuring and $200.4 million aggregate outstanding principal amount of bonds issued in a prior restructuring of interest arrears. See "Public Debt—Debt Crisis and Restructuring—1992 Financing Plan". After giving effect to the cancellation of such bonds, approximately $35.0 billion aggregate principal amount of bonds issued pursuant to the Republic's Brady Plan-type restructuring remained outstanding on April 30, 1999. In 1998, debt service (principal and interest) on public sector external debt was equivalent to approximately $15.4 billion, which amounted to approximately 30.2% of receipts from exports of goods. Throughout the debt restructuring process, from 1982 to 1994, the Republic continued to make principal and interest payments on its external bonded indebtedness in accordance with the terms of such indebtedness. See "Public Debt—Debt Record" and "—Debt Crisis and Restructuring".

SELECTED BRAZILIAN ECONOMIC INDICATORS

	1994	1995	1996	1997	1998
The Economy					
Gross Domestic Product ("GDP"):					
(in billions of constant 1998 *reais*)	R$812.8	R$847.1	R$869.6	R$900.9	R$899.8(15)
(in billions)(1)	U.S.$543.1	U.S.$705.4	U.S.$775.5	U.S.$801.7	R$775.5(15)
Real GDP Growth (decline)(2)	5.9%	4.2%	2.7%	3.6%	(0.1)%
Population (millions)	153.1	155.3	157.5	159.9	161.8
GDP Per Capita(3)	U.S.$3,546	U.S.$4,542	U.S.$4,924	U.S.$5,022	U.S.$4,793(15)
Unemployment Rate(4)	5.06%	4.64%	5.42%	5.66%	7.60%
General Price Index-Domestic Supply (rate of change)(5)	909.6%	14.78%	9.34%	7.48%	1.70%
Nominal Devaluation Rate(6)	613.4%	15.0%	6.8%	n.a.	
Domestic Real Interest Rate(7)	24.2%	33.4%	16.5%	16.1%	26.6%
Balance of Payments (in billions)					
Exports	U.S.$43.5	U.S.$46.5	U.S.$47.7	U.S.$53.0	U.S.$51.1
Imports	33.1	50.0	53.3	59.8	57.7
Current Account	(1.7)	(18.0)	(23.1)	(30.9)	(34.3)
Capital Account (net)	8.7	28.8	34.0	26.0	13.4
Change in Total Reserves(8)	6.6	13.0	8.3	(7.9)	(7.6)
Total Official Reserves	38.8	51.8	60.1	52.2	44.6
Public Finance					
Financial Surplus (Deficit) as % of GDP(9)	(45.5)%	(7.2)%	(5.9)%	(6.1)%	(8.0)%
Primary Surplus (Deficit) as % of GDP(10)	5.3	0.4	(0.1)	(1.0)	0.0
Real Interest Expense as % of GDP	(4.1)	(5.3)	(3.7)	(3.3)	(7.6)
Operational Surplus (Deficit) as % of GDP(11)	1.4	(4.9)	(3.8)	(4.3)	(7.5)
Public Debt (in billions)					
Gross Internal Debt (Nominal)(12)	U.S.$173.1	U.S.$225.3	U.S.$300.4	U.S.$328.0	U.S.$354.2
Gross External Debt (Nominal)(13)	94.6	95.2	94.4	88.5	95.9
Public Debt as % of Nominal GDP					
Net Internal Debt	20.7%	24.9%	29.4%	30.2%	36.0%
Net External Debt(14)	8.5	5.6	3.9	4.3	
Total Public Debt (Nominal)	U.S.$267.6	U.S.$320.5	U.S.$394.8	U.S.$416.5	U.S.$450.1

(1) Converted into dollars based on the weighted average exchange rate for each year.
(2) Calculated based upon constant average 1998 *reais.*
(3) Not adjusted for purchasing power parity.
(4) Average annual unemployment rate of the metropolitan regions of Belo Horizonte, Porto Alegre, Recife, Rio de Janeiro, Salvador and São Paulo. See "The Brazilian Economy—Employment".
(5) GPI-DS is one indicator of inflation. While many inflation indicators are used in Brazil, the GPI-DS, calculated by the Getúlio Vargas Foundation, an independent research organization, is one of the most widely utilized indices.
(6) Year on year percentage devaluation of the *real* against the dollar (sell side).
(7) Brazilian federal treasury securities deflated by the GPI-DS and adjusted at each month-end to denote real annual yield.
(8) Because of the impact of Errors and Omissions and adjustments for valuation/devaluation of other currencies against the dollar, monetization/demonetization of gold and reclassified assets, figures regarding changes in total reserves do not reflect the sum of the Current Account and the Capital Account. See "Balance of Payments and Foreign Trade—Balance of Payments".
(9) Financial results represent the difference between the consolidated public sector debt in one period and the consolidated public sector debt in the previous period, excluding the effects of the Government's privatization program.
(10) Primary results represent Government revenues less Government expenditures, excluding interest expenditures on public debt.
(11) Operational results represent Government revenues less Government expenditures, including interest expenditures on public debt.
(12) Presents debt on a consolidated basis, which is calculated as the gross internal debt less credits between governmental entities.
(13) Not including external private debt. Consolidated external private debt as of December 31, 1998 was U.S.$118.8 billion.
(14) Gross external debt less total reserves.
(15) Estimated.

Sources: Fundação Instituto Brasileiro de Geografia e Estatística (IBGE); Getúlio Vargas Foundation; Central Bank

THE FEDERATIVE REPUBLIC OF BRAZIL

Area and Population

Brazil is the fifth largest country in the world and occupies nearly half the land area of South America. Brazil is officially divided into five regions consisting of 26 states and the Federal District, where the Republic's capital, Brasília, is located.

Brazil has one of the most extensive river systems in the world. The dense equatorial forests and semi-arid plains of the North are drained by the Amazon River and the fertile grasslands of the South by the Paraná, Paraguay and Uruguay Rivers. Other river systems drain the central plains of Mato Grosso and the hills of Minas Gerais and Bahia. Most of the country lies between the Equator and the Tropic of Capricorn, and the climate varies from tropical to temperate. More than half of the total terrain of Brazil consists of rolling highlands varying from 650 to 3,000 feet in altitude.

Brazil's population, estimated at December 31, 1998 to be 161.8 million, is the fifth largest in the world. According to the Brazilian Institute of Geography and Statistics ("IBGE"), the population is currently growing at a rate of 1.3% per year and is expected to reach 166 million by the end of the century. Approximately 79.4% of the population lives in urban areas; the urban population has been increasing at a greater rate than the population as a whole. The largest cities in Brazil are São Paulo and Rio de Janeiro, with populations of 9.8 million and 5.5 million, respectively. Other cities with populations in excess of one million are Brasília, Belém, Belo Horizonte, Curitiba, Fortaleza, Manaus, Porto Alegre, Recife and Salvador. The States with the largest GDP in Brazil, São Paulo, Rio de Janeiro and Minas Gerais, have populations in excess of 33.7 million, 13.3 million and 16.5 million, respectively.

There are approximately 75 million persons of working age in Brazil. The active labor force is composed of 69 million persons, of whom approximately 55.8% work in retail and other services, approximately 24.2% work in agriculture and related areas, and approximately 20.0% work in industry.

Although social welfare indicators in Brazil such as per capita income, life expectancy, and infant mortality do not compare favorably to those of certain of Brazil's neighboring countries, according to recent reports by the International Bank for Reconstruction and Development (the "World Bank") and the United Nations, Brazil has made significant progress in improving social welfare over the past two decades. Between 1970 and 1997 life expectancy in Brazil increased by approximately 13.8% (from 58.7 years in 1970 to 66.8 years in 1997) and the infant mortality rate decreased 61.1% (from 95 per 1,000 live births in 1970 to 37 per 1,000 live births in 1997). Adjusted for purchasing power parity by the United Nations, real GDP per capita rose 1.5% annually from 1975 to 1995. In addition, the reduction in inflation under the *Plano Real* and the consequent diminution of the erosion of purchasing power, as well as significant recent real increases in the legislated minimum wage and renewed economic growth, have improved the social welfare of large numbers of lower-income Brazilians.

The following table sets forth comparative GDP per capita figures and selected other comparative social indicators for 1997:

Table No. 2

Social Indicators, 1997

	Brazil	Argentina	Chile	Ecuador	Mexico	Peru	U.S.	Venezuela
Real GDP per capita(1)	$4,790	$8,950	$4,820	$1,570	$3,700	$2,610	$29,080	$3,480
Life expectancy at birth (years)	66.8	72.9	74.9	69.5	72.2	68.3	76.7	72.4
Infant mortality rate (per 1,000 births)	34	22	11	33	31	40	7	21
Adult literacy rate	84.0%	96.5%	95.2%	90.7%	90.1%	88.7%	—	91.0%

(1) Based on 1997 figures, adjusted for purchasing power parity by the United Nations. Per capita GDP amounts in this chart therefore differ from the amounts for per capita annual income set forth in "Summary Economic Information".

Sources: United Nations Development Program, Human Development Report 1999; World Bank Atlas 1999

Form of Government and Political Parties

Brazil was discovered by the Portuguese navigator Pedro Álvares Cabral in the year 1500 and remained a Portuguese colony for more than 300 years. The colonial government, first established in Salvador in the Northeast, was transferred to Rio de Janeiro in 1763. During the Napoleonic wars the Portuguese court moved from Lisbon to Rio de Janeiro, where it remained until 1821. In the following year Brazil declared its independence from Portugal, and the Prince Regent Dom Pedro I became Emperor of Brazil. His successor, Dom Pedro II, ruled Brazil for 49 years, until the proclamation of the Republic on November 15, 1889. From 1889 to 1930, the presidency of the Republic alternated between officeholders from the dominant states of Minas Gerais and São Paulo. This period, known as the First Republic, ended in 1930, when Getúlio Dorneles Vargas took power. Vargas governed Brazil for the next fifteen years, first as chief of a provisional government (1930-1934), then as a constitutional president elected by Congress (1934-1937) and finally as dictator (1937-1945) of a government that he termed the New State (*Estado Novo*). During the period from 1945 to 1961, Brazil held direct elections for the presidency. The resignation of President Jânio da Silva Quadros in 1961 after less than seven months in office and the resistance to the succession to the presidency of Vice President João Goulart created a political crisis that culminated in the establishment of a parliamentary system of government. The new system of government lasted approximately 16 months. In January 1963, after a plebiscite, Brazil returned to a presidential government, which was overthrown by the military in March 1964. Military governments ruled Brazil from 1964 until 1985, when a civilian president was elected by means of an electoral college composed of Senators and Deputies.

Thereafter, a series of political reforms was enacted, including the reestablishment of direct elections for the President and the calling of a Constitutional Assembly which, in October 1988, adopted a new Brazilian Constitution. In December 1989, Fernando Collor de Mello was elected President of Brazil for a five-year term in the first direct presidential election since 1960. President Collor's political support began to ebb in June 1992, when the National Congress initiated an investigation into charges of corruption involving the President. In December 1992, President Collor resigned from office in the midst of his impeachment trial. The then-Vice President, Itamar Augusto Cautiero Franco, who had become acting President in October 1992 during the impeachment proceedings, assumed the Presidency and remained in office until the end of former President Collor's term on December 31, 1994. On January 1, 1995, the Presidency was assumed by Fernando Henrique Cardoso, who was elected in October 1994 to serve a four-year term. Mr. Cardoso was reelected to a second four-year term in October 1998.

Brazil is a federative republic with broad powers granted to the federal Government. The Constitution provides for three independent branches of government: an executive branch headed by the President; a legislative branch consisting of the bicameral National Congress, composed of the Chamber of Deputies and the Senate; and a judicial branch consisting of the Federal Supreme Court and lower federal and state courts. Amendments to the Constitution require an absolute three-fifths majority vote, in each of two rounds of voting, in both houses of the legislature. A matter addressed in a proposed amendment that is rejected cannot be reproposed during the same legislative session. The Constitution provided for a mandatory constitutional review that began in October 1993 and ended on May 31, 1994. The review resulted in the adoption of six amendments, which included the reduction of the presidential term of office from five to four years and the adoption of the Emergency Social Fund (*Fundo Social de Emergência* or "ESF"). Since January 1, 1995, the National Congress has adopted 18 Constitutional amendments and the Cardoso administration has proposed further revisions. See "The Brazilian Economy—Constitutional Reform". The Constitution also provided for a plebiscite in April 1993 in which voters were permitted to consider alternative systems of government, including a return to monarchy; in that plebiscite, the Brazilian electorate voted overwhelmingly to maintain the presidential system of government.

Under the Constitution, the President is elected by direct vote. A constitutional amendment adopted in June 1997 permits the re-election for a second term of the President and certain other elected officials. The President's powers include the right to appoint ministers and key executives in selected administrative posts. The President may issue provisional measures (*medidas provisórias*) that can be enforced for a maximum of 30 days; they remain in force thereafter only if approved by the legislature within such 30-day period. The prevailing legal view is that the President may re-issue a provisional measure not previously rejected by the National Congress. A proposed constitutional amendment that would impose restrictions on the use of provisional measures was approved by the Senate in two rounds of voting. The proposed amendment must be approved by the Chamber of Deputies to become effective. Under the Constitution, certain legislation submitted by the President must be voted upon by the National Congress within 90 days. In order to be enacted into law, a bill must be approved by both houses of the National Congress and signed by the President.

The legislative branch of government consists of a bicameral National Congress composed of the Senate and the Chamber of Deputies. Ordinary legislation requires only a simple majority vote in both houses of the National Congress for adoption. The Senate is composed of 81 senators, elected for staggered eight-year terms, and the Chamber of Deputies has 513 deputies, elected for concurrent four-year terms. Each State and the Federal District is entitled to three Senators. The number of Deputies is based on a proportional representation system weighted in favor of the less populated States which, as the population increases in the larger States, assures the smaller States an important role in the National Congress.

The following table sets forth by the number and party affiliations of Senators and Deputies in the National Congress as of June 7, 1999.

Table No. 3

Distribution of National Congressional Seats by Party

	Senate	Chamber of Deputies
Partido da Frente Liberal (PFL)	20	110
Partido do Movimento Democrático Brasileiro (PMDB)	26	101
Partido da Social Democracia Brasileira (PSDB)	16	101
Partido dos Trabalhadores (PT)	7	60
Partido Progressista Brasileiro (PPB)	3	50
Partido Democrático Trabalhista (PDT)	3	23
Partido Trabalhista Brasileiro (PTB)	1	22
Others	5	46
Total	81	513

Sources: General Secretariats of the Offices of the Chamber of Deputies and of the Senate and Central Bank

The judicial power is exercised by the Federal Supreme Court (composed of 11 Justices), the Superior Court of Justice (composed of 33 Justices), the Federal Regional Courts (appeals courts), military courts, labor courts, electoral courts and the several lower federal courts. The Federal Supreme Court, whose members are appointed for life by the President, has ultimate appellate jurisdiction over decisions rendered by lower federal and state courts on Constitutional matters.

Brazil is divided administratively into 26 States and the Federal District. The States are designated as autonomous entities within the federative union and have all powers that the Constitution does not preclude the States from exercising. The Constitution reserves to the Republic the exclusive power to legislate in certain areas, including, among others, monetary systems, foreign affairs and trade, social security and national defense. The States may exercise legislative power in matters not reserved exclusively to the Republic and have, concurrently with the Republic, certain powers of taxation. At the State level, executive power is exercised by governors elected for four-year terms and legislative power by State deputies also elected for four-year terms. Judicial power at the state level is vested in the State courts, and appeals of State court judgments may be taken to the Superior Court of Justice and the Federal Supreme Court.

The PFL has the largest delegation in the National Congress, although none of the political parties can be said to play a dominant role. Among the other major parties are the PSDB, the PMDB, the PT, the PPB, the PDT and the PTB.

Federal, State and Local Elections

National general elections were last held on October 5, 1998. The office of the President, two-thirds of the Senate and all of the seats in the Federal Chamber of Deputies, as well as seats in the State legislatures, were determined through the election. Fernando Henrique Cardoso was reelected to a second term of office as President of Brazil in national elections that occurred on October 5, 1998. Mr. Cardoso's second four-year term of office began on January 1, 1999. Mr. Cardoso's party, the Brazilian Social Democratic Party (PSDB), increased the number of its seats in the Chamber of Deputies from 95 to 99 (out of 513), and now holds the second largest number of seats in the coalition of six parties (holding 390 seats) that generally support the Government. In elections for State governors, candidates from parties allied with the government coalition prevailed in 21 of 27 States, including in the State of São Paulo. The opposition won in six States, including Rio de Janeiro and Rio Grande do Sul.

Local elections were last held in 1996. On October 3, 1996, the first stage of local elections was conducted, resulting in the election of the mayors of several major municipalities, including Curitiba, Fortaleza, Porto Alegre, Recife and Salvador. Mayoral contests in certain other major municipalities, such as Belo Horizonte, Florianópolis, Maceió, Rio de Janeiro and São Paulo, were decided in a runoff election, which occurred on November 15, 1996.

External Affairs and Membership in International Organizations

Brazil maintains diplomatic and trade relations with almost every nation in the world. It has been a member of the United Nations since 1945. The Republic participates in the organizations under the control of the United Nations Secretariat, as well as others of a voluntary character, such as the International Fund for Agriculture and Development.

Brazil is an original member of the International Monetary Fund (the "IMF") and the World Bank, as well as three affiliates of the World Bank, the International Finance Corporation, the International Development Association and the Multilateral Investment Guaranty Agency. Brazil was an original member of the General Agreement on Tariffs and Trade ("GATT") and is a charter member of the World Trade Organization. In addition, Brazil is an original member of the Inter-American Development Bank ("IDB"), the Inter-American Investment Corporation and the African Development Bank Group.

At the regional level, Brazil participates in the Organization of American States (the "OAS") and in several sub-regional organizations under the OAS, as well as in the Latin American Economic System, the Latin American Integration Association, the Andean Development Corporation and the Financial Fund for the Development of the River Plate Basin.

In March 1991, Brazil, Argentina, Paraguay and Uruguay entered into the Treaty of Asunción, formally establishing the Mercado Comum do Sul ("Mercosul"), a common market organization composed of the signatory nations. In December 1994, the four member countries signed an agreement establishing the date of January 1, 1995 for the implementation of a Common External Tariff ("CET") intended to transform the region into a customs union. However, because each member country was permitted a list of 450 exceptions (399 in the case of Paraguay) to the CET, the full implementation of a customs union has not been achieved. In December 1995, Mercosul and the European Union signed a framework agreement for the development of free trade between them. In 1996, Mercosul signed agreements with Chile and Bolivia, effective October 1996 and February 1997, respectively, for the development of free trade among them; these agreements were approved by the Brazilian National Congress in September 1996 and April 1997, respectively.

THE BRAZILIAN ECONOMY

Recent Performance

Throughout the 1980s and the early 1990s, the Brazilian economy suffered through periods of high inflation and recession. Until recently, the Brazilian economy has shown improvement in a number of areas. GDP grew in real terms by 3.6% in 1997, 2.7% in 1996, 4.2% in 1995, 5.9% in 1994 and 4.9% in 1993, compared with a decrease of 0.5% in 1992. The industrial sector grew in real terms by 5.8% in 1997, 3.3% in 1996, 1.9% in 1995, 6.7% in 1994 and 7.0% in 1993 compared to a decline of 4.2% in 1992. The service sector grew in real terms by 2.7% in 1997, 2.3% in 1996, 4.5% in 1995, 4.7% in 1994 and 3.2% in 1993. In 1998, however, the Brazilian economy slowed as GDP declined by 0.1%. The services sector grew by 0.8%, while the industrial sector contracted by 1.3%. See "—Gross Domestic Product".

Brazil's exports grew each year from 1991 to 1997. In the five-year period ending December 31, 1997, exports rose from $38.6 billion in 1993 to $43.5 billion in 1994, $46.5 billion in 1995, $47.7 billion in 1996 and $53.0 billion in 1997. Exports, however, declined as a percentage of GDP, from 9.0% of GDP in 1993 to 6.6% in 1997. Imports to Brazil also rose during that period, both in nominal terms and as a percentage of GDP. Imports to Brazil rose from $25.3 billion in 1993 to $33.1 billion in 1994, $50.0 billion in 1995, $53.3 billion in 1996 and $59.8 billion in 1997, an increase from 5.9% of GDP in 1993 to 7.4% of GDP in 1997. The rise in imports contributed to trade deficits of $3.5 billion in 1995, $5.6 billion in 1996 and $6.8 billion in 1997; in 1992, 1993, and 1994, by contrast, Brazil registered trade surpluses of $15.2 billion, $13.3 billion and $10.5 billion, respectively. Because of the decline in economic activity in 1998, Brazil's overall trade flows declined to $108.8 billion that year. Imports declined by 3.5% to $57.7 billion in 1998, while exports declined by 3.5% to $51.1 billion that year. Brazil ended the year with a trade deficit of $6.6 billion. See "Balance of Payments and Foreign Trade—Foreign Trade".

Over the four years ended December 31, 1996, Brazil generally experienced growth in international reserves, which totalled $38.8 billion at year-end 1994, up from $32.2 billion at year-end 1993 and $23.8 billion at year-end 1992. During the first four months of 1995, as a result of a trade deficit, a decline in foreign capital inflows during the first quarter of 1995 and the Central Bank's use of foreign exchange reserves to stabilize the value of the *real* against the U.S. dollar, international reserves declined, reaching $31.9 billion as of April 30, 1995. Thereafter, international reserves exhibited an upward trend, reaching $60.1 billion at the end of December 1996, corresponding to approximately 14 months of imports of goods. In response to a sell-off of Brazilian securities in late October 1997 and related declines in the Brazilian stock markets and an increased demand for foreign exchange, the Government used a portion of its international revenues to intervene in the foreign exchange market; at December 31, 1997, Brazil's international reserves stood at $52.2 billion. Brazil's international reserves recovered during the first four months of 1998, reaching a historical high of $74.7 billion at April 30, 1998. At July 31, 1998, Brazil's international reserves stood at approximately $70.2 billion, corresponding to approximately 14 months of imports. However, in August and September 1998, international reserves came under pressure due to a significant sell-off of Brazilian securities. Although outflows in August 1998 were partially offset by net foreign direct investment, Brazil's international reserves declined to $67.3 billion at August 31, 1998, $45.8 billion at September 30, 1998 and $42.4 billion at October 31, 1998. Brazil negotiated a $41.8 billion IMF-led support package in November 1998 and received the first disbursement (in the amount of $9.3 billion) under that support package in December 1998. After giving effect to that disbursement, Brazil's international reserves stood at $44.6 billion on December 31, 1998. In January 1999, Brazil's international reserves came under significant pressure once again as a result of a series of events that month, including a failed attempt to effect a controlled devaluation of the *real* by widening the band within which the *real* was permitted to trade. The Central Bank subsequently announced that the *real* would be permitted to float, with Central Bank intervention to be made only in times of extreme volatility. After giving effect to a second disbursement (in the amount of $9.8 billion) under the IMF-led support package and a global offering of debt securities by Brazil, the Republic's international reserves stood at

$33.8 billion at March 31, 1999. See "—*Plano Real* and Current Economic Policy" and "Balance of Payments and Foreign Trade—International Reserves". Since reaching its highest quotation of R$0.829 per U.S. dollar on October 14, 1994, the *real* has experienced a cumulative devaluation of 40.3%, reaching R$1.1634 per U.S. dollar on July 31, 1998. On August 31, 1999, the *real*/U.S. dollar exchange rate (sell side) in the commercial exchange market, as published by the Central Bank, was R$1.9159 to $1.00. See "Balance of Payments and Foreign Trade—Foreign Exchange Rates and Exchange Controls".

The inflation rate has declined significantly in recent years. Average monthly inflation, as measured by the GPI-DS, was 43.2% during the first half of 1994 and the monthly rate of inflation reached 46.6% in June 1994. During the second half of 1994, the average monthly rate of inflation declined to 2.65%. This reduction resulted from the implementation of the third phase of the *Plano Real* and occurred without the price, wage or asset freezing mechanisms utilized in prior stabilization programs. See "—*Plano Real* and Current Economic Policy". The sharp decline in the inflation rate during the second half of 1994 contributed to a considerable recovery of domestic demand and coincided with an acceleration of the growth rate of the Brazilian economy. The average monthly rate of inflation has continued to decline, reaching 1.16% in 1995, 0.75% in 1996, 0.60% in 1997 and 0.14% in 1998. The annual inflation rate for 1998 was 1.7%, versus 7.5% in 1997, 9.3% in 1996, 14.8% in 1995 and 909.6% in 1994. The inflation rate has risen in 1999, however, following the decision of the Central Bank in January 1999 to permit the value of the *real* to float against that of the dollar. The inflation rate registered 12.6% for the twelve months ended August 31, 1999. See "—Prices".

While the Brazilian government has been successful in reducing inflation and maintaining economic growth under the *Plano Real*, the Government has yet to complete efforts to reform the country's fiscal imbalance. During 1995, Brazil's public sector operational deficit grew to 4.8% of GDP from a 1994 surplus of 1.3% of GDP. The public sector operational deficits for 1996 and 1997 were 3.8% and 4.3%, respectively, of GDP. The operational deficit resulted from various factors, including higher interest payments on Brazil's growing domestic debt and increased personnel expenses associated with the country's large public sector workforce. Pending the completion of structural reforms, including certain constitutional amendments and other legislation, the Government is taking other measures to reduce the fiscal deficit. See "—*Plano Real* and Current Economic Policy" and "Public Finance—Consolidated Public Sector Fiscal Performance".

Historical Background to Economic Policies

From the late 1960s through 1982, Brazil followed an import-substitution, high-growth development strategy financed, in large part, by heavy recourse to foreign borrowings. Foreign debt grew at an accelerated pace in response to the oil shocks of the 1970s and, when international interest rates rose sharply in 1979-80, the resulting accumulated external debt became one of Brazil's most pressing problems in the decade that followed. See "Public Debt—Debt Crisis and Restructuring". The debt crisis of the 1980s and high inflation substantially depressed real growth of Brazil's GDP, which averaged 2.3% per year from 1981 to 1989. The public sector's role in the economy also expanded markedly, with many key economic sectors subject to Government monopoly or subsidized participation, and significant structural distortions were introduced through high tariffs and the creation of subsidies and tax credit incentives. Significant increases in the money supply to finance a large and growing fiscal deficit further fueled inflationary pressures.

Efforts to address these problems during the late 1980s and early 1990s were largely unsuccessful. High inflation and the recurrent threat of hyperinflation during this period prompted the Government to pursue a series of stabilization plans, but these plans were undermined by a variety of factors. Stabilization measures implemented at that time relied on mechanisms, such as price and wage freezes and/or unilateral modifications of the terms of financial contracts, that were not supported by fiscal and monetary reforms. A central problem during this period was the public sector, which ran operational deficits averaging more than 5% of GDP during the five-year period from 1985 to 1989, while monetary policy was compromised by the short-term refinancing of public sector debt. These problems were aggravated by the 1988 Constitution, which limited the ability of the federal Government to dismiss public sector employees and reallocated public resources, in particular tax revenues, from the federal Government to the States and municipalities without a proportional shift of responsibilities to them, thereby further constraining the effectiveness of federal government fiscal policy. The practice of inflation indexation in the economy, which made prices downwardly rigid, also helped to undermine stabilization measures. See "—Changes in the Relationship between the Federal and Local Governments", "—Employment" and "Public Finance—Taxation and Revenue Sharing Systems".

On February 28, 1986, the Government announced the "Cruzado Plan", a set of measures intended to eliminate inflation by combating inflationary expectations. Among other measures, the Cruzado Plan included a deindexation of the economy, a general wage and price freeze and the replacement of the *cruzeiro* by a new monetary unit, the *cruzado,* which was fixed against the dollar and so designed to eliminate inflationary expectations. Under the Cruzado Plan, inflation initially fell rapidly and the level of the Government's internal debt fell as a result of a substantial increase in the liquidity of the economy that occurred shortly after the implementation of the Cruzado Plan. However, the progressive overvaluation of the *cruzado* against the dollar contributed to a sharp deterioration in Brazil's external accounts, and the Government declared a moratorium on interest payments due on external commercial bank debt in February 1987. A "crawling-peg" exchange rate system, with periodic devaluations, was reintroduced. These adjustments to the Cruzado Plan and subsequent attempts at price freezes and the introduction of a new currency, the *cruzado novo*, proved ineffective in reducing inflation on a sustained basis.

In March 1990, the federal Government, under former President Collor, implemented a new program aimed at restructuring the Brazilian economy and creating the basis for sustained, non-inflationary growth. This program, known as the Collor Plan, included a general 45-day wage and price freeze, the reintroduction of the *cruzeiro* as the national currency and a drastic cutback in liquidity through the Government's retention of approximately one-third of the money supply (measured by M4) or about $34 billion, mainly in the form of private demand deposits, for up to eighteen months. The Collor Plan also called for certain measures that were intended to restrict government expenditures, including the elimination of various semi-autonomous agencies, a cutback of approximately 10% in the number of civil servants and the reduction or elimination of government subsidies.

These stabilization measures resulted in a rapid reduction in the monthly rate of inflation from 81.3% in March 1990 to 9.1% in May 1990. In addition, an increase in the *Imposto sobre Operações Financeiras* (Financial Transactions Tax or "IOF") generated significant tax revenues, transforming a 1989 operational deficit equivalent to 6.9% of GDP into a 1990 operational surplus of 1.3% of GDP. Under the Collor Plan, however, the economy plunged into its most severe recession since 1983, inflation was not reduced on a sustained basis, and public accounts deteriorated again. In response to these unfavorable developments, in January 1991 the Government implemented supplementary measures under the Collor Plan. These measures included the elimination of monetary indexation and most overnight transactions on the federal Government securities market, and the establishment of a new system of calculating interest rates used in the domestic financial market.

A restrictive monetary policy was implemented in the final quarter of 1991, leading to sharp growth in real interest rates and an expansion of domestic savings. These measures had a positive impact on the inflation rate; the rate of price increases stabilized and even began to decline. At the same time, tariffs for public goods and services were increased to eliminate the deficits of the public sector entities providing those services, and the real rate of exchange rose significantly against the dollar.

The approval of a tax reform package in December 1991 increased prospects for an improvement in the fiscal accounts and permitted Brazil to conclude a standby arrangement with the International Monetary Fund. Although monthly inflation began to decline in early 1992, this trend was interrupted in May 1992 because fiscal policy turned out to be weaker than expected and because of uncertainties caused by political developments which later led to the impeachment of President Collor. The Government proposed, but was unable to secure passage of, a series of emergency tax measures, including income tax increases and a broadening of the tax base, to take effect by 1993 in an attempt to reduce the operational deficit.

Nevertheless, substantial progress was made in implementing structural reforms in 1992, particularly with regard to the privatization of public enterprises and trade liberalization. Brazil's balance of payments strengthened markedly in 1992, as the current account shifted to a surplus of 1.6% of GDP, principally reflecting a sharp increase in the trade surplus, and the capital account recorded large inflows, mainly due to high domestic real interest rates and Brazil's renewed access to the international capital markets. As a result, gross international reserves rose from $9.4 billion at the end of 1991 to $23.8 billion at the end of 1992. Also in 1992, Brazil reached agreement on a debt rescheduling with Paris Club creditors and on a comprehensive debt restructuring package with commercial bank creditors providing for debt and debt service reduction. See "Public Debt—Debt Crisis and Restructuring".

Although fiscal policy was restrictive during the first quarter of 1993, public expenditures rose sharply thereafter. In response, the Government introduced the Plan of Immediate Action in mid-June 1993. The Plan included (i) a reduction of Government budgeted current and capital expenditures equivalent to $6 billion, (ii) tax administration measures designed to collect tax arrears and to prevent tax evasion, (iii) the restructuring of debt service obligations of the State and municipal governments to federal financial institutions, (iv) a strengthening of supervision of State banks by restricting their lending to State governments and State enterprises, (v) the restructuring of federal financial institutions, and (vi) steps to expand and accelerate the privatization process.

The primary surplus of the public sector increased from 2.3% of GDP in 1992 to 2.6% of GDP in 1993, and the public sector operational balance shifted from a deficit of 2.2% of GDP in 1992 to a surplus of 0.2% of GDP in 1993. Real GDP grew by 4.2% in 1993 (notwithstanding a slowdown in the latter part of the year), reflecting in part the easing of credit conditions in late 1992 and early 1993.

External sector performance continued to be strong in 1993, although the current account registered a small deficit as a result of a decline in the trade surplus. This reflected a sharp rise in imports induced by the increase in economic activity and further reductions of import duties. The capital account showed continued large inflows, and by the end of 1993 gross international reserves reached $32.2 billion.

Plano Real and Current Economic Policy

In December 1993, the Government announced a stabilization program, known as the *Plano Real*, aimed at curtailing inflation and building a foundation for sustained economic growth. The *Plano Real* is designed to address persistent deficits in the Government's accounts, expansive credit policies and widespread, backward-looking indexation.

The *Plano Real* has three stages. The first stage included a fiscal adjustment proposal for 1994, consisting of a combination of spending cuts and an increase in tax rates and collections intended to eliminate a budget deficit originally projected at $22.0 billion. Elements of the proposal included (i) cuts in current expenditures and investment through the transfer of some activities from the federal Government to the States and municipalities, (ii) establishment of the Emergency Social Fund ("ESF"), financed by reductions in constitutionally mandated transfers of federal Government revenues to the States and municipalities, to ensure financing of social welfare spending by the federal Government, (iii) a prohibition on sales of public bonds by the Government, except to refinance existing debt and for certain specified expenditures and investments, (iv) new taxes, including a new levy on financial transactions, and (v) collection of mandatory Social Security Contributions ("COFINS") in order to finance health care and welfare programs, following the November 1993 confirmation by the Federal Supreme Court that such contributions were permissible under the Constitution.

The centerpiece of the first stage of the *Plano Real* was the creation of the ESF by constitutional amendment in 1994. The ESF enabled the Government temporarily to break certain of the constitutionally mandated links between revenue and expenditure. Pursuant to this amendment, 20% of Government revenues otherwise earmarked for specific purposes were released and deposited into the ESF to ensure financing of social welfare spending by the federal Government for 1994 and 1995. In adopting this constitutional amendment, however, Congress did not modify the existing provisions requiring the federal

Government to share a significant portion of its revenues with States and municipalities. See "—Changes in the Relationship between the Federal and Local Governments".

The second stage of the *Plano Real*, initiated on March 1, 1994, began the process of reform of the Brazilian monetary system. Brazil's long history of high inflation had led to the continuous and systematic deterioration of the domestic currency, which no longer served as a store of value and had lost its utility as a unit of account. Because inflation had reduced dramatically the information content of prices quoted in local currency, economic agents had included in their contracts a number of mechanisms for indexation (providing for the adjustment of the amounts payable thereunder by an agreed-upon inflation or tax rate to preserve the economic value of such contracts) and the denomination of obligations in indexed units of account. The process of rehabilitation of the national currency began with the creation and dissemination of the *Unidade Real de Valor* (the Unit of Real Value, or "URV") as a unit of account. The second stage of the *Plano Real* was designed to eliminate the indexation of prices to prior inflation and to link indexation to the URV instead.

The introduction of the URV was premised on the theory that a reference unit with a nominal value corrected frequently and based on the best estimate of current inflation would express values more realistically than traditional indexing methods, which were based on prior inflation. The URV, therefore, was calculated daily based on estimates drawn from three price indices: the National Consumer Price Index (Extended) developed by the IBGE; the General Price Index (Market) calculated by the FGV and the Consumer Price Index developed by the Institute of Economic Research Foundation ("FIPE"). The URV index was designed to track the loss in the purchasing power of the *cruzeiro real*, the legal currency at the time.

The third stage of the *Plano Real* began on July 1, 1994, with the introduction of the *real* as Brazil's currency. All contracts denominated in URVs were automatically converted into *reais* at a conversion rate of one to one, and the URV, together with the *cruzeiro real*, ceased to exist (although the *cruzeiro real* was generally accepted until August 31, 1994). The *real* initially appreciated against the U.S. dollar, with the rate in the commercial market (selling) moving from R$1.00/dollar, when the *real* was introduced, to R$0.829/dollar on October 14, 1994. Thereafter, the *real* gradually declined in value against the dollar, reaching R$1.1164 per dollar on December 31, 1997 and declining further to R$1.2087 per dollar on December 31, 1998. In March 1995, the Central Bank formalized an exchange band system pursuant to which the *real* would be permitted to float against the U.S. dollar within bands established by the Central Bank. As described more fully below, however, the Central Bank was forced to abandon its exchange band mechanism, which encouraged small exchange devaluations within a specified range, and permit the value of the *real* to float freely against that of the dollar.

Structural reforms proposed by the Government under the *Plano Real* include the transfer of responsibility for certain activities from the federal Government to the States and municipalities, the permitting of private sector participation in certain industries such as petroleum distribution and telecommunications in which public sector entities had monopolies, and tax, administrative and social security reforms. Many of such reforms require amendments to the Constitution, and the Government has thus far been unable to implement all of its proposed reforms. See "—Changes in the Relationship between the Federal and Local Governments" and "—Constitutional Reform". In addition, the privatization of Government-controlled enterprises remains an important element of the structural reform of the Brazilian economy under the *Plano Real*. See "—Constitutional Reform" and "—State-Controlled Enterprises—Privatization Program".

Largely as a result of the measures under the *Plano Real*, the average monthly rate of inflation dropped significantly from 43.2% during the first half of 1994 to 2.65% during the second half of that year. The annual rate of inflation for 1994 was 909.6%, down from 2,708.6% in 1993. The public sector operational balance also showed a surplus of 1.3% of GDP in 1994, versus a 0.2% of GDP public sector operational surplus in 1993. However, the external accounts showed a higher current account deficit in 1994 as a result of an increase in imports and a reduction in net capital account surplus.

In the years following the introduction of the *Plano Real*, the Government was able to make significant gains in reducing inflation. As measured by the GPI-DS, the annual inflation rate in Brazil was 14.8% in 1995, 9.3% in 1996, 7.5% in 1997 and 1.7% in 1998. However, the Government was less successful in reducing imbalances in its fiscal accounts. During 1995, Brazil's public sector operational deficit grew to 4.9% of GDP from a 1994 surplus of 1.4% of GDP. In 1996, the public sector operational deficit, however, was reduced to 3.8% of GDP. Among the measures that contributed to the reduction of the deficit were: (i) the approval of the FEF (see "—Constitutional Reform"), (ii) not indexing increases in the minimum wage or in public sector wages to past inflation, (iii) the significant reduction in the Federal Funds Rate (*taxa Over/Selic*) from an average of 53.09% in 1995 to 27.41% in 1996, thereby reducing the cost of servicing public debt, and (iv) the adoption of the Support Program for the Restructuring and Fiscal Adjustment of the States, which was designed to monitor State and local government spending (see "—Changes in the Relationship between the Federal and Local Governments").

On October 11, 1996, the Government announced a number of measures aimed at combatting the imbalance in federal public sector fiscal accounts over the short term. These measures were implemented through various provisional measures, decrees and resolutions that were intended to reduce significantly the pension and other supplemental employee benefit obligations of the Government, impose limitations on filling vacancies and limit certain overtime and vacation payments. The estimated budgetary impact of the measures was a savings of R$6.5 billion in 1997. On March 5, 1997 the Government submitted to the National Congress a proposed constitutional amendment to extend the life of the FEF until December 31, 1999. The proposed amendment, which was given retroactive effect to June 30, 1997, was adopted on November 25, 1997 as Constitutional Amendment No. 17. Furthermore, the Government implemented several tax reforms, including (i) changes in the reporting and collecting of certain corporate taxes which were expected to result in increased revenues of up to R$3 billion in 1997 and (ii) a new temporary levy on certain financial transactions ("*Contribuição Provisória sobre Movimentação Financeira*" or "CPMF") which became effective on January 23, 1997 for a period of 13 months to assist the Government in funding public health.

In response to a sell-off of Brazilian securities in late October 1997 and related declines in the Brazilian stock markets, the Central Bank took temporary measures designed to provide long-term stability in the Brazilian capital markets and to moderate surges in capital outflows. On October 31, 1997, the Central Bank increased its basic rate, known as the TBC, to 3.05% per month (or 43.4% per annum) from 1.58% per month and its assistance rate, the rate at which the Central Bank lends money to financial institutions in emergencies and known as the TBAN, to 3.23% per month from 1.78% per month. The TBC was reduced to 2.90% per month (or 40.9% per annum) on December 1, 1997, following the approval by the Chamber of Deputies of certain administrative reforms. See "—Constitutional Reform—Administrative Reform". The TBC was further reduced to 38% per annum on January 2, 1998, 34.5% per annum on January 29, 1998 and 28% per annum on March 5, 1998. On November 10, 1997, the Government also announced a package of 51 measures consisting of budget cuts and tax increases intended to reduce the Government's current account deficit in 1998. Measures intended to reduce expenditures included, among other things, (i) a 15% reduction in the 1998 expenditure budget, (ii) layoffs of approximately 33,000 federal workers, (iii) the elimination of 70,000 unfilled federal positions, (iv) a 10% reduction in the number of advisory positions, (v) a reduction of investment in public companies and (vi) a prohibition against federal financing for States that had not signed debt renegotiation accords with the Government. Measures intended to increase revenues included, among others, (i) a 50% reduction in regional and sectorial industrial incentives, (ii) a 10% increase in personal income taxes (IRPF) due in 1998 and a limitation on deductions to 20% of the tax due, (iii) temporary increases in fuel prices and increases in the excise tax (IPI) on automobiles and liquor and (iv) a requirement that State banks pay a greater percentage of profits as dividends to the Government. Certain of these measures, including many spending cuts required Congressional approval for their implementation and were not enacted. Despite these measures, Brazil's public sector operational deficit rose to 4.3% of GDP in 1997 and 7.5% of GDP in 1998.

In 1998, as international reserves once again came under pressure, the Government, among other things, (i) raised the Central Bank's assistance rate (TBAN) to 49.75% from 29.75% per annum, (ii) temporarily eliminated financial institutions' access to funds at the Central Bank's basic rate (TBC), (iii) reduced the minimum term for new foreign currency debt to one year from two years and (iv) reduced the minimum term for the rollover of foreign currency debt to six months from one year. In addition, on October 28, 1998, the Government announced a set of measures, collectively referred to as the Fiscal Stabilization Program, that are intended to produce a primary surplus of 2.6% of GDP in 1999, 2.8% of GDP in 2000 and 3.0% of GDP in 2001. The Fiscal Stabilization Program had two components: (1) structural measures to address the roots of fiscal disequilibrium and (2) the Action Plan for 1999-2001. The structural measures included:

(a) the implementation of the measures included in Constitutional Amendment No. 19 relating to administrative reform (see "—Constitutional Reform");

(b) the proposal and enactment of a fiscal responsibility law that, among other things, established ceilings on public expenditure and indebtedness for all three levels of government and imposed sanctions for noncompliance;

(c) the simplification of the tax system through, among other things, a reduction in the number of taxes collected; and

(d) the reform of the budgetary process.

The Action Plan for 1999-2001 included, among other things,

(i) spending cuts for state enterprises for 1999 of approximately R$2.7 billion,

(ii) extending to retired civil servants the obligation to make social security contributions in an amount equal to 11% of their pensions,

(iii) imposing a 9% supplemental social security contribution on persons earning salaries or receiving pensions over R$1,200 per month for a period of five years,

(iv) extending the provisional financial contribution transaction levy (CPMF), which was due to expire on December 31, 1998, and increasing that tax from the current rate of 0.20% to 0.38% in 1999 and 0.30% in 2000 and 2001,

(v) increasing the contribution for social purposes (COFINS) by one percentage point (to 3% from 2%) and extending the application of that tax to the financial sector, which had previously been exempt, and

(vi) extending the term of the Fiscal Stabilization Fund (FEF) to 2006 and increasing the amount retained by the Government from the present 20% of certain tax revenues to 40% of such tax revenues in 2000 to 2006.

See "—Constitutional Reform—Provisional Financial Contribution Transaction Levy" and "Public Finance —Taxation and Revenue Sharing Systems". The Government estimates for the Fiscal Stabilization Program assumed reduced GDP growth of 0.5% in 1998 and negative 1.0% in 1999.

The Government made some initial progress in implementing the Fiscal Stabilization Program and Action Plan. On November 18, 1998, the National Congress approved four fiscal measures, including the proposed extension to retirees of the obligation to make social security contributions, the proposed increase to 3% of the COFINS rate and the extension of that tax to the financial sector, which previously had been exempt. On November 26, 1998, the Government delivered to the National Congress legislation to simplify the tax system by, among other things, eliminating six existing taxes (including COFINS, the federal tax on industrial products (IPI) and the state tax on the circulation of goods and services (ICMS)) and replacing them with a single value-added tax. The bill also proposed to introduce a permanent federal tax on financial transfers (IMF) to replace the provisional financial contribution levy (CPMF).

In addition, on November 13, 1998, the International Monetary Fund (IMF) announced a $41.8 billion support package for Brazil, approximately $18.3 billion of which is to be provided by the IMF and $4.5 billion by each of the World Bank and the Inter-American Development Bank. An additional $14.5 billion is to be provided by 20 countries through a credit facility coordinated by the Bank for International Settlements and the Ministry of Finance of Japan. Of the support package resources, $32.2 billion would be available to Brazil during the first 12 months, if needed. Brazil received the first installment of approximately $9.3 billion in two disbursements, following the approval of the IMF's component of the support package by its Executive Board on December 3, 1998 and the ratification of the package by the Brazilian Senate.

Brazil's international reserves stabilized following the announcement of the support package, reaching $41.2 billion at November 30, 1998. The Central Bank also lowered the TBAN rate during this time from 49.75% to 42.25% on November 12, 1998 and 36% on December 17, 1998. In December 1998, however, there were significant outflows following the Government's failure to secure passage of a key social security reform bill by the Chamber of Deputies in a December 3, 1998 vote and delays in the voting of the increase of the CPMF rate.

In January 1999, Brazil's international reserves again came under significant pressure as a result of a series of events that month. On January 6, 1999, the newly inaugurated governor of the State of Minas Gerais announced that the State would suspend for 90 days payments in respect of the State's approximately R$18.3 billion debt to the Government. A week later, on January 13, 1999, Gustavo H.B. Franco, the president of the Central Bank and one of the architects of the *Plano Real*, resigned and was replaced by Francisco Lopes, who attempted a controlled devaluation of the *real* by widening the band within which the *real* was permitted to trade. Subsequent Central Bank intervention failed to keep the *real*-U.S. dollar exchange rate within the new band, however, and on January 15, 1999, the Central Bank announced that the *real* would be permitted to float, with Central Bank intervention to be made only in times of extreme volatility. Following that announcement, the value of the *real* against the U.S. dollar declined approximately 21% from its level on January 12, 1999.

To minimize excessive exchange rate volatility and reduce the inflationary effects of the devaluation of the *real*, the Central Bank raised its assistance rate (TBAN) to 41% from 36% on January 19, 1999, and the Central Bank intervened in the market to adjust the Federal Funds Rate (*taxa Over/Selic*) to 32% on January 19, 1999 from 29.8% the previous day. The *Over/Selic* rate was further increased to 35.5% on January 28, 1999 and 37.0% on January 29, 1999. Both the level of international reserves and the value of the *real* continued to decline, however; as of January 31, 1999, Brazil's international reserves stood at $36.1 billion, and the *real*-U.S. dollar exchange rate (sell side) in the commercial exchange market, as published by the Central Bank, stood at R$1.9832 to $1.00.

The Government also continued its efforts to implement the expense reduction and revenue enhancement measures under its Fiscal Stabilization Program. On January 20, 1999, the Chamber of Deputies, reversing its December 3, 1998 vote, approved legislation to extend to retired civil servants the obligation to make social security contributions in respect of their monthly pensions at tax rates ranging from 11% to 25% of the amount of their monthly pensions in excess of R$600. The bill also increased the social security contribution of active civil servants earning more than R$1,200 per month. This legislation, which was approved by the Senate on January 26, 1999, became law on January 28, 1999. Moreover, the Congress approved an austerity budget on January 25, 1999 that provided for spending cuts of approximately R$8.7 billion. In addition, the Chamber of Deputies approved on March 18, 1999, in the second round of voting, a bill that would increase the provisional financial contribution transaction levy (CPMF) to 0.38% from 0.20%. This measure had previously been approved by the Senate. The increased CPMF tax will be collected during the second half of 1999.

On February 2, 1999, when the cumulative devaluation (since January 13, 1999) of the *real* against the U.S. dollar exceeded 40%, the Government designated Armínio Fraga Neto to replace Francisco Lopes as president of the Central Bank. Following Mr. Fraga's confirmation on March 3, 1999, the Central

Bank eliminated the TBC and TBAN rates, giving primacy to the *Over/Selic* rate; because the Central Bank can influence the *Over/Selic* rate on a daily basis through its participation in auctions, repurchase transactions and reverse repurchase transactions, the *Over/Selic* rate permits the Central Bank to react more quickly to changes in market conditions. The Central Bank also increased the *Over/Selic* rate to 45% from 39%. The Central Bank subsequently reduced the *Over/Selic* rate to 42% on March 25, 1999, 39.5% on April 6, 1999, 34% on April 15, 1999, 32% on April 29, 1999, 29.5% on May 10, 1999, 27% on May 13, 1999, 23.5% on May 20, 1999, 22% on June 9, 1999 and 21% on June 24, 1999, citing lower-than-expected inflation and improved expectations for the economy. The *Over/Selic* rate was further reduced to 19.5% on July 28, 1999 and 19% on September 22, 1999.

Following its decision to permit the *real* to float, the Government began negotiations with the IMF on adjustments to the 1999-2001 economic program agreed in November 1998 and new economic targets in light of the new foreign exchange regime introduced in January 1999. On March 5, 1999, Brazil and the IMF announced that they had reached agreement. Under the agreement, Brazil has undertaken to adopt measures designed to achieve primary surpluses, excluding debt payments, of at least 3.1% of GDP in 1999, 3.25% of GDP in 2000 and 3.35% of GDP in 2001, substantially greater than the 2.6%, 2.8% and 3.0% of GDP surpluses for 1999, 2000, and 2001, respectively, under the November 13, 1998 agreement with the IMF. By contrast, Brazil had primary results of -0.1%, -0.9% and 0.0% of GDP in 1996, 1997 and 1998, respectively. The public debt/GDP ratio, currently in excess of 50%, is also targeted to fall below 46.5% at year-end 2001. The Memorandum of Economic Policy annexed to the IMF letter of intent noted that certain of the measures intended to produce the agreed-upon primary surpluses had already been approved or announced, including (i) the suspension until the end of 1999 of PIS/COFINS credits for exports, (ii) an increase in the IOF for consumer lending and (iii) the submission to the Congress of legislation to require military personnel to make contributions to the social security system. Brazil has also agreed to reduce the investment budgets of state-owned companies by 0.9% of GDP, accelerate the privatization of state enterprises and promote the independence of the Central Bank through, among other things, the introduction of fixed terms for the president and directors of the Central Bank. The new agreement anticipated a decline in GDP of approximately 3.5% to 4.0% for 1999, while inflation was expected to increase initially above a 10% per annum rate in the first part of 1999, decreasing gradually during the second half to result in an average monthly inflation rate of 0.5% to 0.7% at year-end 1999. Under the revised program, the trade deficit, which had been projected to be $6.4 billion for 1999, was expected to revert to a surplus of approximately $11.0 billion, and the current account deficit was targeted to fall from 4.5% of GDP to 3.0% of GDP.

On April 6, 1999, Brazil received a second disbursement, of approximately $4.9 billion, from the IMF, which was followed by an additional $4.9 billion in bilateral loans on April 9 1999 under the IMF-led support package. Subsequent disbursements under the IMF's letter of intent will be based on Brazil's ability to meet the primary surplus targets described above and on the Republic's progress in implementing the promised fiscal reforms. There can be no assurance that Brazil will be able to meet the primary surplus targets under its agreement with the IMF and, accordingly, that the full amount under the IMF-led support package will be available to Brazil. See "Public Debt—Debt Crisis and Restructuring".

After giving effect to the inflows from the IMF-led support package and an offering of debt securiities by the Republic in April 1999 (see "Public Debt—Debt Crisis and Restructuring"), Brazil's international reserves stood at $44.3 billion on April 30, 1999, up from $35.5 billion at February 28, 1999 and $33.8 billion at March 31, 1999. The real-U.S. dollar exchange rate (sell side) in the commercial exchange market on April 30, 1999 as published by the Central Bank, stood at R$1.6607 to $1.00, up from R$1.722 to $1.00 on March 31, 1999, and the average real-U.S. dollar exchange rate during January 1999 and February 1999 was R$1.5019 to $1.00 and R$1.9137 to $1.00, respectively, versus R$1.2106 to $1.00 immediately prior to the widening of the trading band.

On June 18, 1999, the Government repaid approximately 30% of the initial disbursement by the Bank for International Settlements and the Ministry of Finance of Japan under the $41.8 billion IMF-led support plan, together with approximately $221.8 million in interest. The remaining 70% was rolled over for another six months.

On July 5, 1999, the Government released the Memorandum of Economic Policy resulting from the IMF's third review of Brazil's performance under the IMF-led support program established in December 1998. The Memorandum reported that the Brazilian economy was performing better than originally forecast. According to the Memorandum, GDP growth fell less rapidly than predicted during the first quarter of 1999, reflecting significant increases in agricultural production; GDP was expected to decline by approximately 1% or less in 1999, versus the 3.5% to 4.0% decline forecast in the March 8, 1999 Memorandum of Economic Policy. In addition, the inflation rate (as measured by IGP-DS) during the first five months of 1999 was 7.4%, versus the 11% rate that had been previously forecast. However, the trade balance continued to show a slight deficit during the first five months of 1999, and the surplus was therefore likely to be lower than projected (approximately $4.0 billion versus the $10.8 billion previously forecast).

The Memorandum left unchanged the primary surplus targets described in the March 8, 1999 Memorandum of Economic Policy but includes inflation targets of 8% in 1999, 6% in 2000 and 4% in 2001, as measured by the IBGE's IPCA index. The Government has also undertaken to continue its efforts to implement fiscal and structural reforms intended to meet the targets under the March 8, 1999 Memorandum of Economic Policy. According to the Memorandum, the Government intends to seek Congressional approval of tne Law of Fiscal Responsibility (which would, among other things, establish ceilings on public expenditure and indebtedness for all three levels of government and impose sanctions for noncompliance) and tax reforms, implement legislation recently approved by Congress that is intended to reduce personnel expenses at all levels of government and work with the Congress to develop new measures to shore up the nation's social security system.

The reduction of inflation resulting from the *Plano Real* made it more difficult for certain financial institutions which had profited from high inflation rates to survive. From the implementation of the *Plano Real* to October 31, 1998, 127 financial institutions, of which nine had assets over $500 million, were the subject of Central Bank intervention; 108 of these troubled institutions have ceased operations. See "The Financial System—General".

Multi-Year Plan 1996/99

In 1995, the Government prepared a multi-year development plan in accordance with Article 165 of the Constitution (the "Multi-Year Plan 1996/99" (*Plano Plurianual*)), which broadly outlines the Government's economic priorities through 1999.

The Multi-Year Plan 1996/99, which assumes the continued success of the *Plano Real* in limiting inflation and fostering economic growth, places a strong emphasis on eliminating barriers to competition in various economic sectors, facilitating privatization, making significant investments in infrastructure development to permit the integration of the less developed areas of Brazil into the modern economy and fostering improved education and social development programs.

Changes in the Relationship between the Federal and Local Governments

The Constitution reallocated public resources from the federal Government to the States and municipalities without a corresponding shift of the responsibility to provide certain essential public services, which remained with the federal Government. The imbalance of resources and responsibilities has been exacerbated by State and local borrowing, particularly during State election campaigns.

As part of the *Plano Real*, and in connection with the creation of the ESF, the Government announced its intention to cut current expenditures and investment through the transfer of certain activities from the federal Government to the States and municipalities. Because certain of these proposals required amendments to the Constitution, they were considered as part of the ongoing constitutional review by the National Congress. Although the National Congress approved the creation of the ESF, other changes sought by the Government were not adopted. The Cardoso Administration has included proposals regarding changes in the relationship between the federal Government and local governments in its political program.

The realignment of spending responsibilities is particularly important for a sustainable solution to Brazil's fiscal problems. Uncommitted revenue of the Government currently does not exceed 20.0% of total revenues, which is insufficient to meet the Government's funding needs with respect to personnel, procurement, investment and debt service. Unless constitutionally mandated transfers to States and municipalities are modified, a portion of any increases in revenue may be automatically translated into new expenditures. See "Public Finance—Taxation and Revenue Sharing Systems".

In addition, supervision of the State banks has intensified as part of the effort to curtail abuses in State and local borrowing. Because of the measures taken to reduce liquidity in the domestic market, certain State-owned and privately owned banks that were dependent on readily available overnight interbank funds have faced liquidity difficulties. On December 30, 1994, authorities from the Central Bank assumed responsibility for the operation of two large State-owned banks, BANESPA and BANERJ. Banco Itaú S.A. has purchased two State banks—BANERJ on June 26, 1997 for R$331.0 million and Banco do Estado de Minas Gerais (BEMGE) on September 14, 1998 for R$583.0 million—and control of BANESPA passed to the federal Government on December 31, 1997 in connection with the restructuring of the State of São Paulo's R$16.8 billion debt to BANESPA. In addition, Banco do Estado de Pernambuco S.A.—BANDEPE was sold to Banco ABN AMRO on November 17, 1998 for R$182.9 million. In addition, the Republic is in the process of liquidating certain other State financial institutions such as Produban, the State bank of Alagoas, and the State banks of Amapá, Mato Grosso and Rio Grande do Norte.

In an effort to correct imbalances in the finances of State and local governments, the Government has introduced initiatives in recent years that have included the rescheduling of State and local debt and the imposition of limits on the incurrence of new debt. In connection with the tax reform package approved by the National Congress in December 1991, the Government agreed to the rescheduling of State debts over a 20-year period and provided for the restructuring of certain bankrupt State development banks. As part of the implementation of the Government's Plan of Immediate Action in June 1993, the National Monetary Council approved a resolution which prohibits federal and State banks from lending money to their main shareholders (the federal and State governments) and which limits credit to the public sector and Central Bank loans to financial institutions through special lines of credit.

All State and most municipal governments completed their debt restructuring agreements (with respect to debt other than bonds) with federal financial institutions in March 1994. The agreements, covering approximately $23 billion in debts, call for a resumption of debt service, limited to 9.0% of specified revenue in 1994 and to 11.0% of such revenue in the second through the twentieth years. In the event that accrued debt service exceeds these limits, the difference is to be capitalized and become payable in the 10 years following the original 20-year term. In return for the resumption of debt service and the conclusion of the restructuring agreements, the States may regain access to federal Government guarantees for foreign borrowings under specified procedures. The objective of the debt restructuring and the introduction of strict limits on other forms of financing by State and municipal governments (for example, a 1993 Constitutional amendment prohibiting virtually any issuance of domestic or foreign securities by State and municipal governments until December 31, 1999, except to refinance existing indebtedness) was to limit the operational deficit of these governments to 0.4% of GDP in 1994 and 1995. Despite those efforts, the combined operational deficits of the State and municipal governments for 1994, 1995, 1996, 1997 and 1998 were 0.6%, 2.3%, 1.8%, 2.3% and 1.8% of GDP, respectively. See "Public Finance".

On December 20, 1995, the Government implemented the Support Program for the Restructuring and Fiscal Adjustment of States, which is aimed at correcting chronic imbalances in the finances of the State and local governments. Under this program, State and local governments were required to comply with targets relating to fiscal balance as a condition for receiving Government financing. The fiscal adjustments to be implemented by the States included the following: (i) reduction and control of personnel costs, (ii) compliance with privatization programs for State enterprises and certain public services in cooperation with BNDES and the appropriate federal ministries, (iii) reform of tax collection systems and implementation of financial controls and budgetary limitations at the State level, (iv) reduction of high levels of State-level indebtedness through restructuring facilities with the National Treasury and (v) the commitment to meet certain minimum fiscal targets (including satisfactory debt/net revenue ratios) as a step towards the balancing of State budgets. Nineteen State governments signed agreements undertaking to implement required policy changes as a condition of receiving specified financial assistance. The total amount of financing disbursed under this program was approximately R$3.3 billion.

On December 19, 1996, the Government issued Provisional Measure No. 1,560 (subsequently enacted as Law No. 9,496 of September 11, 1997), which authorized the federal Government to assist in the refinancing of (i) the public securities debt of the States, (ii) loans made by CEF to the States under various federal measures authorizing temporary financial assistance to the States and (iii) the debt of the States owed to banks controlled by such States. The debt eligible to be refinanced under Law No. 9,496 included debt previously refinanced under the Support Program for the Restructuring and Fiscal Adjustment of States. Each refinancing arrangement was to be subject to the previous approval of both the federal Senate and the respective State Assembly. The refinancing arrangements were required to conform to the guidelines approved by the Government in its Support Program for the Restructuring and Fiscal Adjustment of the States. In addition to specific targets for each State or the Federal District, the refinancing contracts were to require: (i) improvements in the primary fiscal results, (ii) reduction in the expenditures pertaining to civil servants, (iii) achievement of a specific "financial debt/actual net revenue" ratio, (iv) improvement in the collection of State revenues, (v) adoption of privatization programs, concession of public services and administrative reform and (vi) limitation of the ratio of investment expenditure to actual net revenue. As of June 30, 1998, twenty-four States had signed agreements with the Government, covering approximately R$94 billion in debt. On November 27, 1996, the federal Government and the State of São Paulo signed an agreement that provides for, among other things, the restructuring of the State's R$16.8 billion debt to BANESPA as part of a larger restructuring of the State's debt pursuant to Law No. 9,496. Under the agreement, 20% of the State's debt restructured thereunder is to be repaid through the transfer by the State to the federal Government of certain assets to be privatized. The remaining 80% of such State debt is to be paid in monthly installments over a 30-year period. In addition, in November 1997, the Senate passed Resolution No. 118 of 1997, which provided for the restructuring of R$50.4 billion in debt of the State of São Paulo under the Support Program for the Restructuring and Fiscal Adjustment of States. Resolution No. 118 provides, among other things, for the repayment of such debt over a 30-year period plus interest at 6% per annum (adjusted for inflation based on GPI-DS).

On August 18, 1999, the Brazilian Senate adopted Resolution No. 32, authorizing an amendment to the restructuring agreement between the Republic and the State of Santa Catarina under the Support Program for the Restructuring and Fiscal Adjustment of States. The amendment covers obligations of the State to the Social Security Institute of the State of Santa Catarina (*Instituto de Previdência do Estado de Santa Catarina* or IPSEC), which totalled approximately R$514.9 million as of June 30, 1999.

In August 1996, the federal Government issued Provisional Measure No. 1,514 dated August 7, 1996 (subsequently superseded by Provisional Measure No. 1,773-32 dated December 14, 1998) which established a program to facilitate the restructuring of Brazil's State banks. This provisional measure permitted the Republic, in its sole discretion, to (i) acquire control of a financial institution, exclusively for its privatization or dissolution, (ii) finance the closure of the financial institution or its transformation into a non-financial institution or development agency or (iii) finance the prior arrangements necessary for the privatization of the financial institution or to guarantee any credit by the Central Bank for the same end, in accordance with rules to be promulgated by the National Monetary Council. The Republic could also acquire contractual debts owed by a controlling shareholder to the financial institution and refinance the debts so acquired. However, the acquisition and refinancing of such contractual debts and the provision of such partial financing were subject to certain limits. The provisional measure permitted the Republic to finance the acquisition of controlling interests in the State banks and of such contractual debts through the issuance of National Treasury Notes (*Notas do Tesouro Nacional* or "NTNs"). In general, financing or refinancing contracts under the provisional measure were required to be executed on or before June 30, 1998. In exceptional situations, the Government could elect to provide partial financing in order to improve the condition of the financial institution in contemplation of its recapitalization and the introduction of new management with a higher degree of efficiency and professional practices; the deadline for any such financing to be agreed between the federal Government and any controlling shareholder was March 31, 1998. A second exception to the June 30, 1998 deadline applied when the federal Government elected to acquire control of a financial institution for the purpose of privatizing or liquidating that institution; in this case, the deadline for the signing of the relevant financing or refinancing contract was extended to November 15, 1998. As of July 30, 1998, six State banks had been restructured at a cost to the National Treasury of R$6.9 billion.

In February 1997, a Parliamentary Committee of Inquiry (the "CPI") began an investigation of allegations that certain Brazilian States and municipalities may have misused the proceeds of certain debt securities which were issued by such States and municipalities to pay final judgments pursuant to Article 33 of the Constitutional Act of Transitory Dispositions ("Article 33"). On August 19, 1997, the CPI issued a report setting forth recommendations for corrective action. As a consequence of the CPI, the Senate adopted Resolution No. 78 of 1998 on July 1, 1998, which severely restricts the issuance of debt securities by States and municipalities. The total amount of securities of the States and municipalities outstanding as of December 31, 1998 was approximately R$24.3 billion, of which an estimated R$8.6 billion was issued to pay final judgments under Article 33.

On January 6, 1999, the newly inaugurated governor of the State of Minas Gerais announced that the State would suspend for 90 days payments on its approximately R$18.3 billion debt to the Government. The governor of the State of Rio Grande do Sul subsequently sought and obtained an injunction permitting that State to make payments into an escrow account, pending the resolution of the request of seven States to renegotiate refinancing agreements reached with the Government under Law No. 9,496 of September 11, 1997. The Government responded by withholding Constitutionally mandated transfers payable to the State of Minas Gerais and, on February 10, 1999, paid approximately half of an approximately $85 million due in respect of the State's Eurobonds that matured on that date to ease investor concerns about the risk of default by State governments. The Government also notified certain international financial institutions that it would no longer guarantee these States' obligations to these financial institutions, leading the World Bank to suspend loans to the States of Minas Gerais and Rio Grande do Sul.

In a meeting with the President on February 26, 1999, certain of the governors pressed for a renegotiation of the refinancing agreements. The President offered instead to make loans to the States to cover the costs of layoffs and pension reform and promised to review a law exempting exports from State taxes. The Government has initiated negotiations with the World Bank to secure funding for such loans.

On June 2, 1999, the Central Bank declared the State of Pernambuco in default after the State announced that it would not honor approximately R$260 million aggregate principal amount of the State's bonds. As a result of the default, the State is precluded from borrowing in the local markets.

Constitutional Reform

In 1995, the Government proposed certain Constitutional reforms to the National Congress that were intended to reduce public sector involvement in the economy and permit certain industries, especially those that require extensive capital investment, to gain access to foreign capital. Amendments to the Constitution require a three-fifths vote of each house of Congress in two separate rounds. Pursuant to the proposed amendments, matters currently within the ambit of Constitutional law would be transferred to and regulated by ordinary law, thereby granting Congress more regulatory control over the economy. Since January 1, 1995, the National Congress has adopted 18 Constitutional amendments. Some of the major Constitutional amendments approved by the National Congress during the Cardoso Administration are described below.

- *Pipeline Distribution of Gas.* The Constitution had granted States a monopoly over pipeline distribution of gas, entitling them to carry out the service directly or to grant a concession to a State-owned company. The Constitution was amended to permit States to grant concessions to any company, public or private. The amendment became effective on August 15, 1995 (Constitutional Amendment No. 5).
- *Domestic and Foreign Capital.* The Constitution had distinguished between Brazilian companies capitalized from domestic sources (*capital nacional*) and those capitalized from foreign sources (*capital estrangeiro*). The right to drill and explore for mineral resources was limited to Brazilian nationals or companies of *capital nacional.* Similarly, only Brazilian nationals or companies of *capital nacional* had the right to receive royalties as owners of mining deposits or gas or oil fields. As a result of an amendment which became effective on August 15, 1995 (Constitutional Amendment No. 6), the Constitution no longer distinguishes between Brazilian companies based upon the origin of their capital. On June 16, 1999, the Government completed a two-day auction of licenses to explore for oil, mainly off Brazil's Atlantic coast. The winning bidders in the auction included the AGIP unit of ENI Spa of Italy, BP Amoco P.L.C. and Shell of Great Britain, Exxon, Texaco and Amerada Hess Ltd. of the United States and YPF Sociedade Anônima of Argentina. See "—State-Controlled Enterprises—Privatization Program".
- *Shipping.* The Constitution had reserved coastal and inland shipping to Brazilian vessels and required that the owners, the captains and two-thirds of the crew of these vessels be Brazilian citizens. Constitutional Amendment No. 7, which took effect on August 15, 1995, removed these provisions and transferred the rules for coastal and inland shipping to the realm of ordinary law, opening such activities to foreign vessels. On January 8, 1997, Law No. 9,432 was enacted to regulate this sector.
- *Telecommunications.* The Constitution had granted the Republic a monopoly over the telecommunications sector. Constitutional Amendment No. 8, which became effective on August 15, 1995, provides that the Republic may freely grant concessions to private sector companies to provide telephone and telecommunications services and data transmission services. On November 28, 1995, the Government issued three decrees aimed at restructuring the telecommunications sector. The first two decrees established the rules for granting telecommunications services and the range of acceptable frequencies. The third decree relates to cable television concessions. Concession grants depend on the issuance of ordinary legislation which sets forth regulations pertaining to such concessions. On July 19, 1996, President Cardoso signed Law No. 9,295, which includes a provision allowing foreign ownership of up to 49% of cellular, satellite and cable concessions for the three years ending July 19, 1999 and as much as 100% thereafter. Law No. 9,472, which took effect on July 16, 1997, also provides for the privatization of the telecommunications sector and establishes the National Telecommunications Agency (*Agência Nacional de Telecomunicacões*-ANATEL). Pursuant to Law No. 9,295, the Government is completing the auctioning of "Band B" cellular telecommunications licenses to private operators. Under the tender rules published by the Government, ten licenses were to be granted, covering ten regions of the country. As of June 30, 1998, only the license for area 8 (Amazônas, Roraima, Amapá, Pará and Maranhão) remained to be awarded; the license had not been awarded prior to that time because of insufficient interest. In addition, the Republic intends to sell by auction a 15-year concession of mobile cellular service ("SNC"). On July 29, 1998, the Government sold its interest in Telecomunicações Brasileiras S.A. ("Telebrás"), the government-controlled telephone company for approximately $19.0 billion. See "—State-Controlled Enterprises—Telebrás".

- *Petroleum.* The Constitution had granted the Republic a monopoly over research and exploration, refining, importation, exportation and transportation of petroleum. All royalties from natural gas or oil exploration had to be paid to the States, the Federal District and the municipalities. Constitutional Amendment No. 9, which became effective on November 9, 1995, maintained the Republic's monopoly in the petroleum sector, but allowed the Government to contract private companies to carry out activities related to that sector. The amendment removed the prohibition against the receipt by private landowners of royalties related to the ownership of gas or oil fields. Changes have also been approved to permit "risk" contracts for the exploration and production of oil and the formation of joint ventures for oil refining and to terminate the Government's monopoly over the transportation of fuel. Law No. 9,478, which took effect on August 6, 1997, ended the Republic's monopoly in the petroleum sector and created two new regulatory agencies, the National Council on Energy Policy (*Conselho Nacional da Política Energética*) and the National Petroleum Agency (*Agência Nacional do Petróleo*—ANP). On June 16, 1999, the Government completed a two-day auction of licenses to explore for oil, mainly off Brazil's Atlantic Coast. See "—State-Controlled Enterprises—Privatization Program".
- *Fiscal Stabilization Fund.* The Government proposed the creation of the Fiscal Stabilization Fund (FEF) as the successor to the ESF, to be in effect for all of 1996 and for the first half of 1997. The proposed amendment was approved in the second of two votes in the Senate on February 29, 1996. The FEF amendment (Constitutional Amendment No. 10) took effect on March 4, 1996 and expired on June 30, 1997. A second amendment, extending the FEF from June 30, 1997 to December 31, 1999, was adopted on November 25, 1997 as Constitutional Amendment No. 17.
- *Provisional Financial Contribution Transaction Levy.* The Government has imposed the CPMF, a new provisional tax on financial transactions to help fund the national healthcare system. This new levy required a constitutional amendment, which was adopted in October 1996. The tax, which took effect on January 23, 1997, imposes a charge of 0.20% on certain financial transactions for a period of thirteen months. On March 28, 1999, the National Congress approved a bill that would increase the CPMF to 0.38% from 0.20%. The increased CPMF tax will be collected during the second half of 1999.
- *Administrative Reform.* The Government proposed administrative reforms aimed at: (i) improving the efficiency of public administration, (ii) facilitating the balancing of public accounts by granting flexibility to adopt measures for the reduction of personnel, (iii) civil service reform and (iv) improving working conditions. Constitutional Amendment No. 19, which became effective June 4, 1998, among other things, establishes limits for the salary and other compensation of public employees and permits the dismissal of public employees. On February 19, 1997, the Federal Supreme Court ruled in favor of 11 civil servants seeking 29% pay increases that previously had been granted only to members of Brazil's armed services. Execution of the judgment was stayed, pending a ruling by the Federal Supreme Court on the Republic's request for clarification as to whether pay increases received by such civil servants during the relevant period could be taken into account in calculating such civil servants' award. On February 19, 1998, the Federal Supreme Court confirmed its ruling, but permitted the awarded pay increases to take into account, among other things, pay increases previously granted to such civil servants. As a result, many of such civil servants may only receive a small increase, if any. Although the Federal Supreme Court's decision does not legally bind Brazil's lower courts in such cases, it is possible that at least some lower courts will apply the Federal Supreme Court's reasoning or otherwise rule in favor of civil servants seeking pay increases in any additional cases that may be brought. The projected cost to the Government of any adverse determination in any such additional cases cannot now be estimated. The Government may seek legislation to address the issues raised by this case.
- *Social Security Reform.* In March 1995, the President proposed a Constitutional amendment to the National Congress to modify the social security system. This amendment was rejected by the Chamber of Deputies on March 6, 1996. A substitute amendment to the executive branch's Constitutional amendment proposal was approved in the second round of voting by the Chamber of Deputies on July 17, 1996 and was sent to the Senate for consideration. On November 4, 1998,

the Chamber of Deputies approved a revised amendment in a second round of voting. The amendment, now known as Constitutional Amendment No. 20, replaces the current retirement system, which bases eligibility for benefits on length of service, with a system based upon a minimum retirement age, years of service and the amount of money the retiree contributed to the system. The minimum retirement ages are 48 for women and 53 for men (and 55 and 60, respectively, for new civil servants), provided they have made contributions to the retirement system for at least 30 and 35 years, respectively. In addition, notional individual accounts are to be established for participants of both the private retirement system (RGPS) and the public retirement system (RJU-Federal). The establishment of such individual accounts will require the passage of ordinary legislation. The Government has also proposed that the link between a retiree's accumulated contributions and expected pension be tightened.

As a result of the foregoing amendments, certain matters formerly regulated by the Constitution are now to be regulated by ordinary law by the National Congress.

While addressing the fiscal situation through the use of certain techniques at its disposal, the Government has proposed to Congress certain other Constitutional amendments and legislation designed to promote structural changes to maintain fiscal balance on a sustained basis. For example, the Government has proposed tax reforms intended to: (i) simplify the revenue system, (ii) facilitate action against tax evaders, (iii) rationalize the tax system to improve the competitiveness of the Brazilian economy and (iv) permit a fairer social distribution of the tax burden. In an early step in the amendment process, the Government's proposal was approved by the Justice and Constitutionality Commission of the Chamber of Deputies on August 30, 1995. In response to opposition in Congress, the Government is considering proposing as ordinary legislation certain aspects of its constitutional reform package that may be enacted as ordinary legislation. Ordinary legislation requires a simple majority of both houses of Congress for passage.

Gross Domestic Product

Brazil experienced significant rates of growth during the period from 1968 to 1973; real growth in GDP during that period averaged over 11% per year, and that period is often referred to as Brazil's "economic miracle". From 1974 to 1980, the real GDP growth rate declined but still averaged over 7% per annum. The 1980s, by contrast, were a period of generally high inflation, low growth and continuing large budget deficits, as the external debt crisis gave rise to a set of significant economic problems from which the country has yet to recover fully. See "Public Debt—Debt Crisis and Restructuring".

Brazil's economic growth has fluctuated greatly in recent years. The average annual real growth rate of GDP during the nine-year period from 1990 to 1998 was 1.9%, but the real growth rate of GDP was negative in 1990, 1992 and 1998 when it declined 4.3%, 0.5% and 0.1%, respectively. During this period, the services and agricultural sectors each grew at an average rate of 3.0% and 1.6%, respectively, while the industrial sector grew by 1.1%. During 1993, the Brazilian economy recovered; GDP increased in real terms by 4.9%, the industrial sector by 7.0% and the services sector by 3.2%. Agriculture was the only principal sector to decline during 1993, by 0.1%. In 1994, the agricultural sector recovered, registering real growth of 5.5%, due primarily to the record harvest of grain that year, which reached 75.2 million tons. In 1994, the industrial and services sectors grew at rates of 6.7% and 4.7%, respectively, and the GDP grew 5.9%. In 1995, GDP increased by 4.2%, with the agricultural, industrial and service sectors rising by 4.1%, 1.9% and 4.5%, respectively. In 1996, GDP increased in real terms by 2.8%, with agricultural, industrial and service sectors rising by 3.1%, 3.3% and 2.3%, respectively. GDP rose 3.6% in real terms in 1997; during that year, the industrial and service sectors grew by 5.8% and 2.7%, respectively, while the agricultural sector declined by 0.2%. The economy slowed in Brazil in 1998, with GDP declining by 0.1%. The industrial sector declined by 1.3% in 1998, while the service sector rose by 0.8%. The agricultural sector remained stable in 1998 (−0.02%).

During the first six months of 1999, Brazil's GDP declined by 0.4% compared to the same period in 1998. The decline in GDP was lower than originally forecast, largely as a result of agricultural output, which grew by 1.6% during the second quarter of 1999, compared to the same period in 1998.

The following table sets forth Brazil's GDP at current prices and expenditures for each of the years indicated.

Table No. 4

Gross Domestic Product at Current Prices—In Billions of Reais (R$)(1)

	1994		1995		1996		1997		1998	
	R$	%	R$	%	R$	%	R$	%	R$	%
Final Consumption	270.6	77.5	513.6	79.5	630.8	81.0	699.4	80.9	732.3	81.4
Gross Capital Formation	77.3	22.2	144.0	22.3	163.0	20.9	187.6	21.7	191.4	21.3
Gross Fixed Capital Formation	72.5	20.8	132.8	20.5	150.1	19.3	172.2	19.9	179.2	19.9
Changes in Inventories	4.9	1.4	11.3	1.8	12.9	1.7	15.3	1.8	12.3	1.4
Exports of Goods and Services	33.2	9.5	49.9	7.7	54.4	7.0	65.5	7.6	66.9	7.4
Less: Imports of Goods and Services	32.0	9.2	61.3	9.5	69.3	8.9	88.3	10.2	90.3	10.1
Gross Domestic Product	349.2	100.0	646.2	100.0	778.8	100.0	864.1	100.0	899.8	100.0

(1) The information in this table has been restated to reflect the current methodology used by IBGE to calculate GDP; prior to 1995 IBGE calculated GDP at constant 1980 prices rather than at current prices.
Source: IBGE

The following tables set forth the participation of classes and activities in value added at basic prices and real growth at basic prices by sector for each of the years indicated.

Table No. 5

Participation of Classes and Activities in Value Added at Basic Prices(1)

	1994	1995	1996	1997	1998
Agriculture	9.9%	9.0%	8.3%	7.9%	8.4%
Industry	40.0	36.7	34.7	34.8	34.0
Mining, Oil and Gas	1.0	0.9	1.0	0.9	0.6
Manufacturing	26.8	23.9	21.5	21.3	20.3
Construction	9.2	9.2	9.5	10.0	10.3
Public Utilities	3.0	2.7	2.7	2.7	2.7
Services	64.3	60.7	62.3	62.4	62.8
Retail Services	9.5	8.9	7.8	7.7	7.3
Transportation	3.5	3.4	3.0	3.0	3.0
Communications	1.5	1.5	1.9	2.1	2.6
Financial Services(2)	15.9	8.0	6.3	6.6	6.5
Government	15.2	16.3	16.0	15.3	15.5
Other Services	18.7	22.5	26.7	27.8	27.9
Total	114.1	106.4	105.1	105.1	105.2
Adjustment(3)	14.1	6.4	5.3	5.1	5.2
Value Added at Basic Prices	100.0	100.0	100.0	100.0	100.0

(1) The information in this table has been restated to reflect the current methodology used by IBGE and the Central Bank to compare the various sectors of the Brazilian economy and the changes therein; prior to 1995 IBGE and the Central Bank calculated the composition of GDP by sector rather than the participation of classes and activities in value added at basic prices.
(2) Does not include financial intermediation services.
(3) Adjustment for double counting arising from the inability to allocate debt service among the classes and activities set forth in this table.
Sources: IBGE and Central Bank

Table No. 6

Real Growth (Decline) at Basic Prices by Sector

	1994	1995	1996	1997	1998
Real GDP	5.9%	4.2%	2.7%	3.6%	(0.1)%
Agriculture and Livestock	5.5	4.1	3.1	(0.2)	0.0
Industry	6.7	1.9	3.3	5.8	(1.3)
Mining, Oil and Gas	6.2	3.7	6.0	6.8	8.0
Manufacturing	7.0	2.0	2.1	4.2	(3.7)
Construction	7.0	(0.4)	5.2	8.7	1.4
Public Utilities	4.2	7.6	6.0	5.8	3.7
Services	4.7	4.5	2.3	2.7	0.8
Retail Services	9.4	8.5	1.8	2.3	(4.5)
Transportation	4.1	6.6	2.6	4.2	2.1
Communications	13.9	22.9	10.9	2.0	6.0
Government	0.4	0.8	1.4	2.4	2.0
Other Services	5.5	3.6	2.3	2.5	(0.6)

Sources: IBGE

Principal Sectors of the Economy

Until the 1950s, natural resources and agriculture were the major sectors in the Brazilian economy. Beginning in the mid-1950s and during the 1960s and 1970s, however, emphasis was placed on industrial development, financed in part by external debt. As a result, the contribution of manufactured goods to Brazilian export revenues has increased significantly, reaching 15.0% in 1970, 44.8% in 1980 and 55.0% in 1995.

Services. During the period from 1990 to 1998, the subsectors that experienced the greatest growth were communications, which grew by 158.2%, and transportation, which grew by 49.9%. During 1994, overall growth in the service sector was 4.7% as a result of increases in communications (13.9%), retail services (9.3%) and transportation (4.1%). In 1995, the subsectors of communications and retail services increased by 22.9% and 8.5%, respectively. Overall growth in the service sector reached 4.5% in 1995 and 2.3% in 1996. In 1997, this sector grew 2.7% mainly as a result of increases in transportation (4.2%) and retail services (2.3%). In 1998, overall growth in the service sector reached 0.8% as a result of increases in transportation (2.1%) and communications (5.9%). Retail services declined 4.5%.

Brazil's road network is comprised of approximately 1.8 million kilometers, about 10% of which is paved. Most paved roads are maintained by federal and State authorities, while the vast majority of unpaved roads are the responsibility of local authorities. Brazil's railway system consists of approximately 30,500 kilometers, of which 7% is electrified. The principal Brazilian cities are served by both domestic and international airlines, and many smaller communities benefit from scheduled service by domestic airlines. Brazil has major ports in Rio de Janeiro, Santos, Paranaguá, São Sebastião and Rio Grande. Brazil also enjoys an extensive coastline and navigable rivers, but the potential of river and maritime shipping has not been fully exploited. Certain broad goals were established for the recovery, modernization and maintenance of the transportation system in the Multi-Year Plan 1996/99. The Government has recently taken initiatives to improve highway, railway and shipping infrastructure, which had deteriorated extensively during the 1980s. The process of privatization of the operation and maintenance of certain highways has begun.

In March 1996, the Government carried out the first of a planned series of auctions of leases to operate the different federally owned portions of the national railway system; the fifth auction took place in December 1996. In July 1997, the Republic completed the privatization of *Rede Ferroviária Federal S.A.*

("RFFSA"), the national railway system, with the sale of *Rede Ferroviária Federal S.A.—Malha Nordeste.* See "—State-Controlled Enterprises—Privatization Program". To date, concessions for the operation of the railway lines covering 21,659 kilometers have been auctioned for a total of $1.5 billion.

As of February 28, 1999, Brazil had approximately 22.9 million telephone lines, including conventional and cellular telephone systems. The network is run by concessionaires in each State which are subsidiaries of Telebrás. Since the late 1980s, considerable investment has been made in the expansion of the services of Telebrás, including the establishment of cellular telephone systems in all of the States and the first fiber optic communications connection between the cities of Rio de Janeiro and São Paulo, which largely accounts for the recent significant growth in the communications sector. The Multi-Year Plan 1996/99 contemplates the institutional restructuring of the communications sector with the aim of opening up the sector to competition. One of the specific targets of the restructuring is to increase the current number of telephone lines to 33 million by the end of the decade. Part of that anticipated increase will be accomplished through the expansion of cellular telephone service. On July 19, 1996, President Cardoso signed a law that will permit the Government to auction to private sector companies licenses to build and operate cellular telephone systems. Pursuant to that law, the Government is completing the auctioning of "Band B" cellular telecommunications licenses to private operators. See "—Constitutional Reform—Telecommunications". In addition, on July 29, 1998, the Government sold its interest in Telebrás for approximately $19.0 billion. See "—State-Controlled Enterprises—Telebrás".

Industrial Production. Industrial production registered a real average annual increase of 1.1% during the nine-year period from 1990 through 1998. Although industrial production declined by 4.2% in real terms in 1992, it increased in real terms by 7.0% in 1993, 6.7% in 1994, 1.9% in 1995, 3.3% in 1996 and 5.8% in 1997. As a result of a slowdown in economic activity in Brazil in 1998, industrial production declined by 1.3% that year. The following table sets forth growth in real terms in the principal areas of industrial production for the periods indicated:

Table No. 7

Annual Changes in Industry Production
Mining and Manufacturing

	1994	1995	1996	1997	1998
Mining, Oil and Gas	4.7%	3.3%	9.8%	7.2%	12.4%
Manufacturing Industry	7.8	1.7	1.1	3.6	(3.3)
By Segment					
Nonmetallic Minerals	3.1	4.1	6.3	7.4	(0.5)
Metallurgy	10.2	(1.8)	1.6	6.0	(3.8)
Machinery	21.1	(4.5)	(12.8)	7.2	(4.0)
Electronic and Communications Equipment	19.0	14.6	4.7	(1.8)	(10.2)
Transportation Equipment	13.4	4.1	(0.3)	10.7	(14.6)
Wood	(2.6)	(3.4)	2.1	3.9	(6.0)
Furniture	1.2	6.2	13.7	(1.5)	(8.2)
Paper and Cardboard	2.8	0.4	2.9	2.9	0.7
Rubber	4.0	(0.3)	(0.5)	4.1	(8.1)
Leather and Hides	(4.3)	(16.7)	(1.9)	(1.7)	(13.6)
Chemicals	6.6	(0.5)	5.0	5.1	3.9
Pharmaceutical Products	(2.5)	18.1	(8.6)	11.4	4.0
Perfumes, Soaps and Candles	2.5	5.3	4.1	5.2	3.1
Plastics	4.1	9.7	11.3	3.6	(2.5)
Textiles	3.8	(5.8)	(5.8)	(6.5)	(6.8)
Clothing, Footwear and Cloth Goods	(2.1)	(6.9)	(2.5)	(6.7)	(4.6)
Food Products	2.2	7.7	5.3	1.0	1.4
Beverages	10.4	17.2	(3.3)	(0.3)	(2.2)
Tobacco	(14.8)	(5.1)	12.5	22.2	(22.7)
Total Annual Change in Production of Mining, Oil and Gas and Manufacturing Industry	7.6	1.8	1.7	3.9	(2.1)
By Category of Use					
Capital Goods	18.7	0.3	(14.1)	4.8	(2.5)
Intermediate Goods	6.5	0.2	2.9	4.6	(0.7)
Consumer Goods	4.4	6.2	5.3	1.2	(5.4)
Durable Goods	15.1	14.5	11.2	3.5	(19.6)
Nondurable Goods	1.9	4.2	3.7	0.5	(1.1)

Sources: IBGE and Central Bank

After experiencing growth of 7.8% in 1994, 1.7% in 1995, 1.1% in 1996 and 3.6% in 1997, the manufacturing industry declined by 3.3% in 1998. In 1994, the capital goods, durable consumer goods and intermediate goods sectors showed growth of 18.7%, 15.1% and 6.5%, respectively. In 1995, durable goods production increased by 14.5% and nondurable goods production increased by 4.2%, while capital goods production expanded by 0.3%. The drop in capital goods growth in 1995 is attributable in large part to a 48.2% increase in capital goods imports that year. The durable consumer goods and intermediate goods sectors continued to grow in 1996 and 1997, increasing 11.2% and 2.9%, respectively, in 1996, and 3.5% and 4.6%, respectively, in 1997. Capital goods production during this period showed an uneven trend, however, declining by 14.1% in 1996 before rising 4.8% in 1997. In 1998, all sectors declined, including durable goods (by 19.6%) and capital goods (by 2.5%). See "Balance of Payments and Foreign Trade—Foreign Trade".

Among the factors accounting for the growth in the manufacturing industry in 1993, 1994 and 1995 were:

- previously idle installed capacity, which allowed the industrial sector to accommodate increasing retail sales;
- an increase in agricultural income as a result of favorable harvests during 1991, 1992 and 1994, which led to increased investment in farm equipment. In 1995, the production of grains increased by 5.4%, according to IBGE;
- a 1994 increase in consumer spending following real wage increases, and after July 1994, the recovery of consumer demand due to the decline of inflation; and
- an agreement, negotiated by automotive industry representatives, the Government and industry workers, whereby retail auto prices were reduced in exchange for wage reductions and decreased taxes.

The relatively slower rate of growth of manufacturing in 1995 is attributable mainly to the tight monetary policy introduced in the context of the *Plano Real.* After a decline in the first half of 1996, due in large part to a reduction of credit to finance purchases of consumer goods, industrial production recovered during the second half of the year and showed a net increase of 1.7% in 1996. The durable consumer goods segment registered the biggest increase (11.2%), followed by non-durable consumer goods (3.7%). This performance was mainly due to the increase in sales on credit and the continued growth in real terms of wages and salaries. Capital goods fell in 1996 (-14.1%), mainly reflecting the increase in imports related to this segment.

In 1997, the growth in manufacturing occurred principally in the areas of capital goods and intermediate goods, due to the rise in investments in machinery and agricultural supplies and by the increase in construction. Growth in the durable goods segment, which led industrial growth in prior years, slowed in 1997, largely as a result of the deceleration in real gains in wages and salaries, the impact of price reductions and reduced access to financing.

In 1998, after five years of growth, manufacturing declined by 3.3%. The largest reduction occurred in the durable consumer goods segment (which declined by 19.6%), principally in automobile and electrical appliances, largely as a result of the maintenance of interest rates at a high level.

Construction sector activity increased 7.0% in 1994. Construction sector activity declined slightly (by 0.4%) in 1995, but thereafter rose by 5.2% in 1996, 8.7% in 1997 and 1.4% in 1998. The number of housing starts in a given year has depended heavily upon the availability of public funds and the ability of the Housing Finance System, currently under the direction of the Federal Savings Bank (*Caixa Econômica Federal* or "CEF"), to devote resources to new building activities. As of December 31, 1998, the credit operations of CEF related to the housing sector totalled R$47.2 billion. The modest growth of the construction sector in 1995 is attributable in part to restrictive monetary policy that year and consequent high interest rates. Moreover, the legislation introducing the *real* as the lawful currency and prohibiting its indexation to inflation for periods shorter than one year diminished the supply of private real estate financing and, consequently, new construction.

Brazil's proven mineral resources are extensive and have generally remained constant or expanded in recent years due to continuing exploration activity. Large iron ore and manganese reserves provide important sources of industrial raw materials and export earnings. Deposits of nickel, tin, chromite, bauxite, beryllium, copper, lead, tungsten, zinc and gold, as well as lesser known minerals, continue to be mined. As other sectors of the Brazilian economy have grown, the mining, oil and gas industry's contribution to industrial production has remained relatively stable, decreasing slightly from 1.6% in 1991 to 0.6% of GDP in 1998. The mining, oil and gas industry grew an average of 3.1% annually from 1990 to 1998. In 1997 and 1998, the mining, oil and gas industry grew 6.8% and 8.0%, respectively.

Agriculture. Brazil has a well-diversified agricultural sector. It is the world's second largest producer of sugar and soya, and from 1994 through 1995 produced approximately 44.1% of the orange juice concentrate in the world market. Approximately 70% of Brazil's sugar crop is processed into alcohol for automotive fuel. Brazil's largest single export crop is soya (beans, bran and oil), with 1996 exports totalling approximately $4.5 billion. In addition, Brazil has been the world's largest producer of coffee for more than a century. Coffee exports totalled $2.1 billion during 1996. In addition, during 1996, meat and meat by-product exports totalled $1.5 billion, orange juice exports $1.4 billion, sugar exports $1.5 billion.

In 1990, a restrictive farm credit policy and a contraction in domestic demand led to a 3.7% decline in real output of the agricultural sector. A subsequent increase in Government funding in this sector led to real growth of 1.4% in 1991 and 4.9% in 1992. In 1993, real output of the agricultural sector declined 0.1% but recovered in 1994, registering a growth rate of 5.5% due to an increase of 6.5% in crops. In 1995, the agricultural sector grew by 4.1% due to a 12.0% increase in livestock. Crop production was stable in 1995. In 1996, the real output of agricultural sector grew 3.1% due to a 3.6% increase in crops. Livestock production rose by 2.4%. The agricultural sector output declined by 0.2% in 1997, due largely to a decline of 1.9% in livestock production. In 1998, the output of the agricultural sector was stable.

On July 20, 1996, President Cardoso ordered the expropriation of 15,000 hectares (37,000 acres) of private land as part of a massive land reform program. The program ultimately aimed to redistribute 11.2 million hectares (26.7 million acres) of land throughout the country from large landowners to some 380,000 landless farming families, many of them current or past squatters, by 1998. This program seeks to resolve the recurring land disputes over the past 10 years between landowners and squatters. By law, owners must be paid fair compensation for the land taken by the federal Government. In the period from 1995 to 1998, 287,539 families were settled on 2,356 lots created by INCRA during those years. During the same period, 7,321,270 hectares of unproductive land were appropriated from large landholders. Loans granted to settlers to fund planting, harvesting and investments totalled more than R$1.2 billion. Another R$35 million of emergency loans are expected to be made in 1999 to settlements affected by the drought in the Northeast.

State-Controlled Enterprises

The public sector grew very rapidly during the 1970s and continues to play a significant role in Brazil's economy. However, the Government and certain State governments have taken steps to reduce their direct and indirect control of state-owned enterprises and to permit privately owned entities to compete with such enterprises. See "—Privatization Program".

In Brazil there are two types of state enterprises: public companies and mixed-ownership companies.

Public companies are corporations wholly owned by the States or the Republic, created by special law to carry on economic activities in any of the corporate forms provided for by law. Examples of federal public companies are BNDES, CEF, the Brazilian Post Office and Telegraph Corporation (*Empresa Brasileira de Correios e Telégrafos*) and the Mineral Resources Exploration Company (*Companhia de Pesquisa de Recursos Minerais* or "CPRM").

Mixed-ownership companies are in corporate form and are majority-owned by the federal Government. Unless otherwise provided by the law authorizing the creation of a mixed-ownership company, the rights of the Government are those conferred by Brazilian corporate law on majority shareholders generally. Brazil's most important non-financial mixed-ownership companies include *Petróleo Brasileiro S.A.* ("Petrobrás") and *Centrais Elétricas Brasileiras S.A.* ("Eletrobrás").

Brazil also has autonomous institutions and public foundations. Autonomous institutions are entities established to carry out public functions which require decentralized financial and operating management, such as the Central Bank, the National Securities Commission (*Comissão de Valores Mobiliários* or "CVM"), the Brazilian Institute of Forest Development, the National Institute of Industrial Property, the National Highway Department and the National Department of Mineral Production.

Public foundations are non-profit public law entities created to carry out activities not performed by public companies. Public foundations have administrative autonomy and manage their own assets, but their expenses are defrayed by the Government and other sources. Examples of public foundations are IBGE, *Instituto de Pesquisa Económica Aplicada* (IPEA) and *Conselho Nacional de Desenvolvimento Científico e Tecnológico* ("CNPq").

Under Brazilian law, private parties may only participate in activities considered to be public services if they are authorized to do so by the Federal Government. The areas formerly reserved to the Republic under the Constitution include broadcasting and telecommunications, electric power service and facilities, hydroelectric power generation, certain interstate and international navigational services, interstate and international highway passenger transportation services and the operation of ports. The mining and processing of nuclear mineral ores and minerals and their by-products also remain under Government monopoly. Amending the Constitution in order to facilitate privatization and competition is an important element of the *Plano Real.* See "—Constitutional Reform" and "—Privatization Program".

The following table sets forth the Government's ownership interest in, and the total assets, net worth, gross sales and net income for the year ended December 31, 1997 of Petrobrás, Eletrobrás and Telebrás:

Table No. 8

Selected State Owned Enterprises(1)
Direct and Indirect Ownership of Government

	Voting	Total	Total Assets	Net Worth	Gross Sales	Net Income(2)
			(in millions of reais, except percentages)			
Petrobrás	86.83%	61.44%	R$38,204	R$21,055	R$30,126	R$1,511
Eletrobrás	80.88	71.36	97,090	61,647	8,763	3,378
Telebrás(3)	50.04	21.32	47,597	31,295	20,698	3,900

(1) Consolidated financial statements, including holdings and subsidiaries, according to the methodology set forth in "Price and Accounting System" (CVM Instruction No. 191, dated July 15, 1992).
(2) Shareholders as a group are entitled to a compulsory dividend equal to at least 25.0% of adjusted net income for the year.
(3) Telebrás was privatized on July 29, 1998. See "—Telebrás".
Source: Ministry of Planning and Budget

Petrobrás. Petrobrás, the largest corporation in Brazil and one of the largest in South America, in terms of consolidated revenues, had a monopoly established by the Constitution over the production, importation and refining (but not distribution) of petroleum in Brazil. All members of its Board of Directors are appointed by the President of the Republic. Constitutional Amendment No. 9, approved on November 9, 1995, maintains the Republic's monopoly in the petroleum sector but permits the Government to contract private companies to carry out activities related to the petroleum sector. The amendment also removes the prohibition against the receipt by private landowners of oil and gas royalties.

Eletrobrás. Eletrobrás is a holding company for the Brazilian electricity sector, with majority shareholdings in four subsidiaries and minority shareholdings in other State utility companies. Eletrobrás acts as the central financing entity for the Brazilian electricity sector and is also responsible for implementing the planning, coordination and supervision of programs for the construction, expansion and operation of electricity generation, transmission and distribution systems, as well as energy conservation programs. It advises the Ministry of Mines and Energy in relation to the establishment of long-term expansion policies for the electric power sector. In May 1995, the Government announced the inclusion of Eletrobrás and its generation subsidiaries, Furnas, Eletronorte, Eletrosul and Chesf, in the privatization program. Eletrobrás' former subsidiaries, *Escelsa* and *Light Serviços de Eletricidade (Light)*, located in the States of Espírito Santo and Rio de Janeiro, respectively, had previously been included in the program. Controlling interests in *Escelsa* and *Light* were sold on July 11, 1995 and May 21, 1996, respectively.

Telebrás. Telebrás, through its various operating companies, was the primary supplier of public telecommunications services in the Republic and owned 94% of all public exchanges and 91% of the nationwide network of local telephone access lines. Its services and rates were subject to comprehensive regulation by the Ministry of Communication in conjunction with the Ministry of Finance. In furtherance of the privatization effort envisioned in the *Plano Real*, the Constitution was amended (Constitutional Amendment No. 8) to permit the Republic to grant concessions to private parties to provide telephone and telecommunications services and data transmission services. On November 28, 1995, the Government issued three decrees aimed at restructuring the telecommunications sector. In addition, the Government enacted a law on July 19, 1996 that permits it to auction licenses to private sector companies to build and operate cellular telephone systems. Pursuant to that law, the Government is completing the auctioning of "Band B" cellular telecommunications licenses to private operators. See "—Constitutional Reform—Telecommunications". On July 29, 1998, the Government completed the privatization of Telebrás in an auction that raised approximately $19.0 billion, 64% above the minimum price established by the Government. In connection with the privatization, Telebrás was divided into twelve companies: three regional fixed-line companies, eight companies providing "Band A" cellular services covering the same areas as the competing "Band B" concessions currently being sold (with the exception of the State of São Paulo, which will form one "Band A" area and two "Band B" areas, as described above) and Embratel, an existing company which provides long-distance and international service. Among the winners in the auction were: a consortium led by Telefónica de España S.A., which acquired three of the companies (including Telesp, the São Paulo fixed line business) for approximately $5.0 billion; Portugal Telecom, which purchased the São Paulo cellular business for $3.1 billion; and MCI, which bid $2.3 billion for Embratel.

Others. In addition, the Government owns a majority of the voting shares of a number of banks, including Banco do Brasil. See "The Financial System—Public Financial Institutions".

Privatization Program. The objectives of the Government's privatization program are to (i) reduce the role of the state in the economy and allocate more resources to social investment, (ii) reduce public sector debt, (iii) encourage increased competition and thereby raise the standards and efficiency of Brazilian industry and (iv) strengthen the capital markets and promote wider share ownership. In 1993, the federal Government proposed constitutional amendments to permit private participation in the state-controlled petroleum and telecommunication sectors. The proposed amendments were not adopted during the constitutional review that concluded on May 31, 1994, but amendments similar in substance were approved by Congress in 1995. See "—Constitutional Reform".

The Privatization Council *("Conselho Nacional de Privatização")*, a body directly subordinate to the President, along with BNDES, is responsible for administering the privatization program. The privatizations have, for the most part, been effected through share auctions conducted on Brazil's stock exchanges. As set forth in the table below, through December 31, 1998, a total of 66 state enterprises or divisions thereof had been privatized, and several minority interests held by government companies had been sold, for consideration totalling $46.2 billion.

Table No. 9

Brazilian Privatization Program

	Month of Auction	Purchase Price(1) (in millions of dollars)
Usinas Siderúrgicas de Minas Gerais S.A.—Usiminas	October 1991	$ 1,941.2
Companhia Eletromecânica—Celma	November 1991	91.1
Material Ferroviário S.A.—Mafersa	November 1991	48.8
Companhia Siderúrgica do Nordeste—Cosinor	November 1991	15.0
Serviço de Navegação da Bacia do Prata—SNBP	January 1992	12.0
Indag S.A.	January 1992	6.8
Aços Finos Piratini S.A.	February 1992	106.6
Petroflex-Indústria e Comércio S.A.	April 1992	234.1
Companhia Petroquímca do Sul—Copesul	May 1992	861.5
Companhia Nacional de Alcalis—Can	July 1992	81.4
Companhia Siderúrgica de Tubarão	July 1992	353.6
Nitriflex S/A Indústria e Comércio	August 1992	26.2
Fertilizantes Fosfatados S/A	August 1992	182.0
Polisul Petroquímica S/A	September 1992	56.8
Companhia Ind. de Polipropileno S/A	September 1992	59.4
Goiás Fertilizantes S.A-Goiasfertil	October 1992	13.1
Companhia de Aços Especiais Itabira—Acesita	October 1992	465.4
Companhia Brasileira de Estireno—CBE	December 1992	10.9
Poliolefinas S.A.	March 1993	87.1
Companhia Siderúrgica Nacional—CSN	April 1993	1,495.3
Ultrafértil S.A. Ind. e Comércio de Fertilizantes	June 1993	205.6
Companhia Siderúrgica Paulista—Cosipa	August 1993	585.7
Aços Minas Gerais S.A.—Açominas	September 1993	598.5
Oxiteno S.A. Indústria e Comércio	September 1993	53.9
Petroquímica União S.A.—PQU	January 1994	287.5
Arafértil S.A.	April 1994	10.8
Mineração Caraíba S.A.	July 1994	5.8
Acrilonitrita do Nordeste S.A.—Acrinor	August 1994	12.1
Companhia Pernambucana de Borracha Sintética-Coperbo	August 1994	25.9
Polialden Petroquímica S.A.	August 1994	16.7
Ciquine Companhia Petroquímica	August 1994	23.7
Politeno Indústria e Comércio S.A.	August 1994	44.9
Empresa Brasileira de Aeronáutica S.A.—Embraer	December 1994	192.2
Sale of minority interests held by government companies	Nov.-Dec. 1994	395.5
Centrais Elétricas do Espírito Santo S.A.—Escelsa	July 1995	519.3
Companhia Industrial de Polipropileno S.A.—Copene	August 1995	270.4
Companhia Petroquímica de Camaçari—CPC	September 1995	99.6
Salgema Indústrias Químicas S.A.	October 1995	139.2
Companhia Química do Recôncavo—CQR	October 1995	1.7
Nitrocarbono S.A.	December 1995	29.6
Pronor Petroquímica S.A.	December 1995	63.5
Companhia Brasileira de Poliuretano—CBP	December 1995	0.04
Polipropileno S.A.	February 1996	81.2
Koppol Filmes S.A.	February 1996	3.1
Rede Ferroviária Federal S.A.—Malha Oeste	March 1996	63.4
Light Serviços de Eletricidade S.A.	May 1996	2,270.9
Deten Química S.A.	May 1996	12.1
Rede Ferroviária Federal S.A.—Malha Centro-Leste	June 1996	316.1
Polibrasil S.A. Indústria e Comércio	August 1996	99.4
Rede Ferroviária Federal S.A.—Malha Sudeste	September 1996	870.6
Estireno do Nordeste S.A.	September 1996	16.6
Rede Ferroviária Federal S.A.—Malha Tereza Cristina	November 1996	17.9
Rede Ferroviária Federal S.A.—Malha Sul	December 1996	208.5
Sale of minority interests held by government companies	December 1996	33.4
Companhia Vale do Rio Doce—CVRD	May 1997	3,298.9
Rede Ferroviária Federal S.A.—Malha Nordeste	July 1997	14.6
TECOM 1Porto de Santos	September 1997	251.1
Banco Meridional	December 1997	240.1
Sale of minority interests held by government companies	Feb.-July 1997	189.6
"Band B" cellular telecommunications licenses	October 1998	7,613.0
Telecomunicações Brasileiras S.A.—Telebrás	July 1998	18,944.0
Sale of minority interests held by government companies	Apr.-Dec. 1998	421.4
Companhia Docas do Espirito Santo-Cais de Capuaba	May 1998	26.2
Companhia Docas do Espirito Santo-Cais de Paul	May 1998	9.4
Tecon 1—Porto de Sepetiba	September 1998	79.0
Centrais Geradoras do Sul do Brasil S. A.—Gerasul	September 1998	879.5
Porto do Rio (Terminal Roll-on Roll-off)	November 1998	26.5
Porto de Angra dos Reis	November 1998	7.9
Rede Ferroviária Federal S.A.—Malha Paulista	November 1998	205.8
Total		$46,168.3

(1) The purchase price does not reflect actual dollars received. In most cases, the purchase price was paid in the form of Brazilian currency or various debt obligations of the Republic, its agencies or state-controlled enterprises redeemed at face value for purposes of these sales. Values in Brazilian currency were converted to U.S. dollars at the commercial selling rate on the closing date following the relevant auction.

Source: BNDES

The legal measures establishing the *Plano Real* provide that Government-held shareholdings in public companies not included in the national privatization program be transferred to the custody of an entity called the Public Debt Amortization Fund to the extent that such shareholdings are not needed to maintain Government monopolies or national control of such companies. Proceeds from the sale of these shares are to be applied directly to the repayment of internal debt of the National Treasury.

In 1995, the Government initiated planning for privatization of electric utilities and rail transport services. In February 1995, the *Lei de Concessões de Serviços Públicos* (Public Services Concessions Law) was enacted, permitting investment in the electricity sector and other sectors considered public services by private companies or individuals. In addition, the Government has enacted a law permitting independent, third-party producers of electricity to compete with the State monopolies, and regulations to implement this law are being formulated. Within the electricity sector, controlling interests in *Escelsa* and *Light* were sold on July 11, 1995 and May 21, 1996, respectively. Banco Meridional, the first federal bank to be slated for privatization, was sold in December 1997 for $240.0 million.

During 1996, the Government (i) began the privatization of 17 hydroelectric projects and certain ports, (ii) approved the privatization of *Companhia Nordestina de Sondagens e Perfurações* (CONESP), (iii) created the National Agency of Electric Energy (*Agência Nacional de Energia Elétrica*—ANEEL) which is charged with regulation of the electricity sector and the preparation of this sector for privatization and (iv) leased or auctioned over 10,000 kilometers of its railway lines.

In 1996, federal privatization revenues totalled R$4.1 billion, of which the *Light* sale accounted for 58% and the RFFSA networks accounted for 36%. The 1996 proceeds represented nearly 30% of the aggregate privatization proceeds obtained since the implementation of the program in 1991.

For the first time in 1996, foreign capital played an important role in the privatization process. Almost $1.4 billion of foreign capital was invested, more than the aggregate amount of the foreign investment previously received on account of privatizations since 1991.

The Government has continued its efforts to reduce its role in the Brazilian economy. On May 6, 1997, the Government sold 41.73% of the voting shares of *Companhia Vale do Rio Doce* ("CVRD"), the world's largest producer and exporter of iron ore, to a consortium led by the Brazilian steelmaker, *Companhia Siderúrgica Nacional* (CSN), for approximately R$3.3 billion, approximately 20% more than the minimum price established by the Government. An additional 5.1% of the total capital stock of CVRD having a value of R$179.0 million was subsequently offered to employees in the second stage of the CVRD privatization. In addition, the Government sold approximately 10% of the total capital stock of *Light* to the company's employees for R$254.1 million in May 1997. The Republic also completed, in July 1997, the privatization of RFFSA with the sale of *Rede Ferroviária Federal S.A.—Malha Nordeste*. A consortium led by the Vicunha group agreed to pay R$15.8 million for the right to operate *Malha Nordeste*, a 37.8% premium over the minimum price established by the Government. Of that amount, R$6.6 million was paid in cash on July 25, 1997, with the remainder of the purchase price to be paid in 108 four-month installments, beginning July 25, 2000. In August 1997, the remaining Ecelsa shares were sold for R$119.0 million, and in September 1997, Terminal 1 of the Port of Santos was privatized for R$254.0 million.

The Government's 1997 budget proposal projected privatization revenues of $5.5 billion during the 1997 fiscal year. Actual privatization revenues for 1997 exceeded expectations, totaling more than $26.0

billion, surpassing aggregate privatization revenues for the period from 1991 through 1996. For the 1998 fiscal year, the Government's budget proposal projected privatization revenues of $13.0 billion. Actual privatization revenues for 1998 totalled $37.5 billion.

In addition to the privatization program, the Government has sought to reduce the regulation of economic activity generally. Important developments in this regard include the establishment of a free foreign exchange market, the reduction of tariffs and elimination of most non-tariff trade barriers and the termination of most price controls. The Government has also acted to deregulate certain segments of the economy, including fuel and oil derivatives, airlines, shipping and steel, and is considering introducing additional measures designed to increase competition in areas such as steel, highway maintenance and transportation, areas which were previously controlled, in most cases, by government enterprises.

In July 1997, the National Congress enacted a new telecommunications law which, among other things, provides for the establishment of a bidding process for concessions for telecommunications services, creates a National Telecommunications Agency to regulate and control the telecommunications sector, permits companies awarded such concessions to set prices after three years of operation and authorizes the President of the Republic to establish by decree limits on the participation of foreign capital in the newly created companies resulting from the privatization of Telebrás. As of December 31, 1998, no such presidential decree had been issued.

The Government also ended the 44-year monopoly enjoyed by Petrobrás in oil exploration with the passage of Law No. 9,478 of August 6, 1997. On June 16, 1999, the Government completed a two-day auction of licenses to explore for oil, mainly off Brazil's Atlantic coast. The winning bidders in the auction—which included the AGIP unit of ENI Spa of Italy, BP Amoco P.L.C., British Borneo and Shell of Great Britain, Exxon, Texaco, Amerada Hess Ltd. and Unocal Latin American Ventures Ltd. of the United States, YPF Sociedade Anônima of Argentina and Petrobrás—agreed to pay a total of $181 million for the licenses awarded in the auction.

The Memorandum of Economic Policy of March 8, 1999 describes a continuing effort to reduce the role of public sector financial institutions in the Brazilian economy. In addition to previously announced plans for the privatization of BANESPA, the Bank of the State of São Paulo currently under federal administration, and of the privatization of the State-owned bank of Bahia, the Government has requested a report on the future role of the federal banks, including Banco do Brasil, S.A., CEF and BNDES.

Privatization of State-Owned Enterprises. The process of privatization in the various States was begun in 1996. Although the aggregate privatization proceeds from the State privatization programs were relatively modest at $1.13 billion in 1996, as of December 31, 1998, fifteen states had enacted privatization legislation: Alagoas, Bahia, Espírito Santo, Goiás, Maranhão, Mato Grosso, Mato Grosso do Sul, Pará, Paraíba, Piauí, Rio de Janeiro, Rio Grande do Sul, Rondônia, São Paulo and Sergipe. The State of Rio de Janeiro completed the sale of a 70.26% interest in its electricity company (*Companhia Energética do Rio de Janeiro*—CERJ), on November 20, 1996 for $587.4 million. In December 1996, the State of Paraná also completed auctions for the concession of the load transportation service in the Paraná Oeste Railroad for $24.8 million. Also in 1996, the State of Rio Grande do Sul sold a 35% interest in its telecommunications company (*Companhia Riograndense de Telecomunicações* (CRT)) for $654.4 million.

The States have continued to privatize public-sector enterprises. On July 14, 1997, the State of Rio de Janeiro sold controlling interests in *Companhia Estadual de Gás* (CEG) and *Riogás* for R$622.2 million, representing a 74.9% premium over the minimum price set by the State. CEG was purchased by a consortium composed of two Spanish companies (Gas Natural SDG and Iberdrola Investimentos), Enron International, a U.S. concern, and Pluspetrol, an Argentine company. *Riogás*, a subsidiary of CEG, was purchased by Gas Natural SDG and two subsidiaries of Enron International, which will share control of *Riogás* with BR Distribuidora, a subsidiary of Petrobrás. In addition, on July 31, 1997, the State of Bahia completed the sale of 65.4% of the voting shares of its electricity company (*Companhia Elétrica da Bahia* —Coelba) for approximately R$1.73 billion, about 77.4% more than the minimum price fixed by Bahia's government. Moreover, on November 5, 1997, a consortium known as VBC purchased a controlling interest in *Companhia Paulista de Força e Luz* (CPFL) for approximately R$3.02 billion, approximately 70.1% above the minimum price set by BNDES and the highest price paid for a single State-owned company. CPFL, which is Brazil's fourth largest distributor of electricity, serves the State of São Paulo. In 1997, privatization revenues from the sale of State-controlled enterprises totaled $11.2 billion, approximately 89% of which arose from dispositions of companies in the energy sector.

State privatization revenues from the inception of the State privatization programs through December 31, 1998 totalled R$27.7 billion, which includes R$3.5 billion in revenues arising from the sale by States of minority interests in government companies.

On April 14, 1999, in the first privatization auction following the decision of the Government to permit the value of the *real* to float against that of the dollar, the State of São Paulo sold a controlling interest in *Companhia de Gás de São Paulo* (*Comgás*) for R$1.6 billion, representing a premium of approximately 119% over the minimum price set by the State. *Comgás* was purchased by a consortium composed of British Gas PLC and Royal Dutch/Shell Group.

Other privatizations of State-owned assets included the sale of Baneb, the State-owned bank of Bahia, to Banco Bradesco S.A. for R$260 million on June 22, 1999 and the sale of Paranapanema, an electricity generation company owned by the State of São Paulo, to Duke Energy on July 28, 1999 for R$1.24 billion, a 90% premium over the minimum price set by the State.

Prices

Brazil experienced high and chronic inflation for many years, which hindered investment and economic growth and contributed to income inequality. Inflation and certain Government measures taken to combat inflation have had significant negative effects on the Brazilian economy generally and on the fiscal accounts of the Government and its ability to service its external debt. See "—Historical Background to Economic Policies".

The following table sets forth two principal price indices for the periods indicated.

Table No. 10

General Price Index—Domestic Supply (GPI-DS)(1)
Wholesale Price Index—Domestic Supply (WPI-DS)

		GPI-DS		WPI-DS	
Period		Monthly	Trailing 12 Months	Monthly	Trailing 12 Months
1993	December		2,708.55		2,639.27
1994	December		909.61		857.75
1995	December		14.78		6.39
1996	December		9.34		8.09
1997	December		7.48		7.78
1998	December		1.70		1.51
1999	January	1.15	1.97	1.58	2.35
	February	4.44	6.48	6.99	9.66
	March	1.98	8.33	2.84	12.64
	April	0.03	8.51	(0.34)	12.58
	May	(0.34)	7.89	(0.82)	11.51
	June	1.02	8.68	1.35	12.82
	July	1.59	10.83	2.03	15.82
	August	1.45	12.64	2.15	18.35

(1) GPI-DS is an index based on a weighting of three other indices: WPI-DS (60%), the Consumer Price Index ("CPI") (30%), and the National Index of Building Costs ("NIBC") (10%).

(2) Annual figures for each month from January 1999 represent trailing 12-month inflation rates.

Sources: Getúlio Vargas Foundation and Central Bank

Chronic inflation in Brazil led to the emergence of a comprehensive system of indexation. Indexation mechanisms were first introduced in 1964, when the monetary correction of certain financial assets was instituted by law. Later, these indexation mechanisms were gradually adopted by all sectors of the economy. Various price indices were developed, each one with its own methodology, based on different baskets of goods or services, such as salaries, rents, taxes and financial instruments. The practice of widespread indexation in Brazil diminished the distorting impact of inflation on relative prices but also served to sustain and fuel inflationary expectations.

Throughout the 1980s Brazil experienced periods of severe inflation. With the onset of the external debt crisis in 1982 and the resulting decrease in the availability of foreign capital, the Government was obliged to monetize large and growing public sector deficits, thereby further stimulating inflation. See "Public Debt—Debt Crisis and Restructuring".

In March 1990, the inflation rate, as measured by GPI-DS, reached 81.3% per month. The adjustment measures related to the Collor Plan announced on March 15, 1990 led to a drop in the monthly inflation rate to 9.1% in May 1990. With gradual relaxation of price controls under the Collor Plan, the inflation rate rose to an average monthly rate of 12.5% in the third quarter of 1990 and 16.5% in December 1990, resulting in an annual inflation rate of 1,476.6% for 1990. See "—Historical Background to Economic Policies".

In 1991, accumulated annual inflation declined to 480.2%. In August 1992, the inflation rate, which had stabilized at approximately 21-22% per month from May through July 1992, accelerated again, in part because of increasing uncertainty about the economic implications of the prospective impeachment of President Collor. Accumulated annual inflation in 1992 was 1,158.0%.

In 1993, wage adjustments, increases in the price of public services, and rising farm prices contributed to the further acceleration of inflation, from a monthly rate of 28.7% in January 1993 to one of 36.2% in December 1993. Accumulated annual inflation in 1993 was 2,708.6%.

In the early months of 1994, increases in food prices and price mark-ups in anticipation of the introduction of the *real* further fueled inflation. Prices during the first six months of 1994 rose at an average monthly rate of 43.2%.

Since the implementation of the third phase of the *Plano Real*, including the introduction of the *real*, in July 1994, the rate of inflation has decreased significantly. See "—*Plano Real* and Current Economic Policy". The high monthly rates of the first half of 1994 have fallen to single digits. Residual inflation from the end of the first half of 1994 resulted in a monthly inflation rate of approximately 5.5% for July 1994. The gradual decline of the impact of these factors resulted in a decreasing inflation rate, which fell to 1.55% for the month of September 1994.

In the second half of 1994, price indices were influenced by increases in rents and the prices of personal services. Up to October 1994, seasonal factors negatively affected the price of farm products, while in the last two months the situation was reversed. The growth of imports of consumer goods helped hold inflation down. Accumulated annual inflation in 1994 was 909.6%.

Accumulated annual inflation in 1995 was 14.8%. This relatively low rate of inflation compared to prior years was due in part to restrictive monetary policy, the widespread availability of competitively priced imported products, and only limited increases in the price of food.

Notwithstanding the gradual reduction of monetary constraints, the inflation rate declined to 9.3% in 1996, 7.5% in 1997 and 1.7% in 1998. The most important factor was the slowdown in wholesale prices, especially in industrial products. The most significant inflationary pressures came from agricultural prices, housing (rent) expenditures, education and health, as well as unit construction costs (mainly manpower).

The inflation rate has risen in 1999, following the decision of the Central Bank in January 1999 to permit the value of the *real* to float against that of the dollar. The inflation rate registered 12.6% for the twelve months ended August 31, 1999.

Following the decision to permit the *real* to float freely, the Government announced that it intends to pursue a monetary policy based on inflation targeting. In June 1999, the Government announced inflation targets of 8% in 1999, 6% in 2000 and 4% in 2001, as measured by the IBGE's IPCA index. See "—*Plano Real* and Current Economic Policy".

Salaries and Wages

Wage adjustments that lagged behind the rate of inflation under the successive economic plans implemented by the Government caused a significant reduction in the real purchasing power of wages during the early 1990s. According to the Employment Monthly Survey conducted by IBGE in six major metropolitan regions of Brazil (Rio de Janeiro, São Paulo, Belo Horizonte, Porto Alegre, Recife and Salvador), the real average wages of all workers declined by 9.4% in 1990, 17.0% in 1991 and 7.9% in 1992. Wages recovered in 1993 and 1994, with real average wages rising by 9.4% and 5.9%, respectively. In 1995, 1996 and 1997, real wages continued to rise, registering increases of 10.4%, 7.4% and 2.1%, respectively. However, real wages declined by 0.4% in 1998.

In 1994, real average wages and overall real wages in the State of São Paulo increased 9.0% and 6.4%, respectively, due to both general economic growth and wage negotiations. In 1995, real average wages and overall real wages in the State of São Paulo continued to rise, registering increases of 8.8% and 7.2%, respectively, for the year. In 1996 and 1997, real average wages increased 5.5% each year, and overall real wages rose 1.3% in 1997 after a decline of 3.7% in 1996. Real average wages increased by 4.6% in 1998, but overall real wages fell that year by 0.9%.

As of May 1, 1999, the national minimum monthly wage was increased by 4.6% to R$136 from R$130. The following table sets forth certain data on wages in the State of São Paulo and on the National Minimum Wage for the periods indicated.

Table No. 11

Industrial Wages—State of São Paulo(1)
and
National Minimum Wage

December 31,	Real Average Wages Index(2)(3)	Trailing 12 months(2)	Real Overall Wages Index(2)(3)	Trailing 12 months(4)	Dollar Equivalent Minimum Wage (monthly)	Dollar Equivalent Minimum Wage Index(3)	Trailing 12 months(4)
1994	130.79	8.99	103.89	6.37	82.35	108.99	(0.84)
1995	137.04	8.78	101.20	7.15	103.31	136.72	33.49
1996	141.19	5.50	98.01	(3.67)	107.97	142.90	8.29
1997	148.91	5.48	99.26	1.22	107.76	142.62	1.33
1998	159.74	4.62	99.74	(0.86)	107.85	142.74	0.27

(1) Information is provided for the State of São Paulo because it represents approximately 44.7% of the industrial production of Brazil.

(2) Deflated by CPI-FIPE.

(3) 1989 average = 100.

(4) Average percentage growth in last 12 months compared to previous 12 month period.

Sources: Federação das Indústrias do Estado de São Paulo ("FIESP"), Ministry of Finance and Central Bank

Employment

The Ministry of Labor customarily reports Brazilian employment statistics in terms of formal employment. Formal employment comprises employment duly registered with the Ministry of Labor and subject to social security contributions by employers. Informal employment is not registered or subject to employment contributions. The Ministry of Labor's General File of Employed and Unemployed showed that formal employment decreased by 2.8% in 1992, resulting in approximately 648,000 lost jobs. Formal employment increased 0.7% in 1993, or by about 154,000 new jobs. In 1994, formal employment increased 1.3%, or by about 274,000 jobs. In 1995, formal employment decreased 1.7%, reflecting a loss of about 412,149 jobs. In 1996, 1997 and 1998, formal employment decreased 1.21%, 0.42% and 2.7%, respectively, or by about 304,950 jobs, 121,892 jobs and 581,753 jobs, respectively.

The table below sets forth employment levels by sector for the periods indicated.

Table No. 12

Level of Employment by Sector(1)

Sector	December 31, 1994	1995	1996	1997	1998
Manufacturing	109.57	104.68	102.05	100.00	94.28
Public Utility/Industrial Services(2)	115.76	110.04	105.31	100.00	93.02
Commerce	99.71	99.26	98.86	100.00	98.62
Services	101.08	100.66	100.08	100.00	99.11
Construction	104.01	100.89	99.41	100.00	95.82
Government Service	100.65	100.59	100.29	100.00	99.86
Total	103.43	101.65	100.42	100.00	97.34

(1) December 31, 1997 = 100.
(2) Including water, electricity, telephone and gas services.
Sources: Ministry of Labor and Central Bank

The Government currently has no comprehensive national unemployment statistic because of the difficulties of measuring the informal employment sector. The Government instead measures unemployment using the average annual rate of unemployment in six major metropolitan areas (Rio de Janeiro, São Paulo, Belo Horizonte, Porto Alegre, Salvador and Recife). According to that measure, unemployment rose in 1992 to 5.8% from the 4.8% rate registered in 1991. The unemployment rate declined slightly in 1993, 1994 and 1995, reaching 5.3%, 5.1% and 4.6%, respectively. In 1996, 1997 and 1998, the level of unemployment increased, reaching 5.4%, 5.7% and 7.6%, respectively.

Unemployment rates declined during the second half of 1998 from 8.02% in July 1998 to 6.32% in December 1998. After rising to 7.73% in January 1999, unemployment rates declined to 7.54% in July 1999, compared with an unemployment rate of 8.02% in July 1998. A large part of the rise in unemployment was attributable to a decline in the level of economic activity as a result of certain of the economic measures taken by the Government to stabilize the value of the *real*. See "—*Plano Real* and Current Economic Policy". The Fiscal Stabilization Program includes measures to reduce the impact of rising unemployment, such as increased benefits for the long-term unemployed, greater flexibility in work contracts and initiatives to create job opportunities for young citizens. However, the Government expects GDP to decline by 1% in 1999, which may result in further increases in the unemployment rate.

The Federal Senate passed a bill on January 21, 1998 permitting employers to offer labor contracts to temporary workers for periods of up to 24 months, providing employers with greater flexibility in dealing with their labor needs. The cost of temporary employees is significantly lower than the cost of permanent employees, who are often entitled to extensive social security, unemployment and severance benefits.

Law No. 7,988, which was enacted on November 1, 1990, established the Workers' Support Fund ("*Fundo de Amparo ao Trabalhador*" or "FAT") to finance unemployment security programs and professional training programs that are expected to benefit about 4.2 million workers between 1994 and 1998. To be eligible for the unemployment benefits under FAT, a dismissed employee, among other things, (i) must have been employed and receiving a salary during the six-month period prior to being dismissed, (ii) must have been employed at least 15 months during the two years prior to being dismissed, (iii) must not be receiving any other social security or unemployment benefits and (iv) must not have sufficient income to support herself or her family. Unemployment benefits under FAT are limited to four months in each sixteen-month period following a dismissal.

FAT received funding of R$3.4 billion and R$4.4 billion in 1994 and 1995, respectively, all from PIS/PASEP contributions. In accordance with Law No. 7,988, 40% of the funds provided for FAT is allocated to finance economic growth programs managed by BNDES. As of December 31, 1995, FAT registered a deficit of R$743 million. Excluding on-lending to BNDES in the amount of R$1.728 billion, FAT would have registered a primary surplus of R$985 million.

The table below sets forth recent industrial employment indices for the State of São Paulo, national employment indices and unemployment rates for the six major metropolitan regions for the periods indicated.

Table No. 13

Employment and Unemployment(1)

	Industrial Employment in São Paulo(2)	% Growth in Year(3)	National Employment(4)	% Growth in Year(5)	Average Unemployment Rate (IBGE)(6)
1994	79.51	(1.09)	93.88	1.25	5.06
1995	73.95	(7.00)	92.27	(1.72)	4.64
1996	69.51	(6.00)	91.15	(1.21)	5.40
1997	66.81	(3.88)	90.77	(0.42)	5.66
1998	62.54	(6.40)	88.36	(2.66)	7.60

(1) Through end of period.
(2) *Source: FIESP.* The index measures employment in the industrial sector in the State of São Paulo, at the end of the relevant period. 100 = annual average for 1989. Figures are provided for the State of São Paulo because it represents 44.7% of the industrial production of Brazil.
(3) *Source: Central Bank.* This column sets forth the growth of industrial employment in São Paulo.
(4) *Source: Ministry of Labor.* This index measures nationwide employment of workers whose employment is governed by the Consolidated Labor Laws, at the end of the relevant period, based on data on employment changes required by law to be reported by employers. 100 = annual average for 1989.
(5) *Source: Central Bank.* This column sets forth the growth of national employment.
(6) *Source: IBGE.* Annual averages of the average monthly rates for the period from 1994 to 1998 and average rates over the relevant period for the metropolitan areas of Rio de Janeiro, São Paulo, Belo Horizonte, Porto Alegre, Salvador and Recife.

Unions and Labor Protection

Under the Constitution, professional or union associations may be freely organized. There are no government formalities for the organization of a union, other than registration at the appropriate agency, and public authorities are prohibited from intervening in or interfering with unions. No more than one union may be created to represent the same professional or economic group in the same geographic area.

Under Brazilian law, the principal function of a union is to represent the general interests of its members as a group or individually. It may also enter into collective labor agreements and promote conciliation in collective labor disputes. The union must provide free legal assistance for its members. A union may not be affiliated with any international organization other than the International Labor Organization unless authorized by the President of the Republic. Union representatives are also protected under Brazilian labor laws. A candidate for a union leadership position or job-safety monitor may not be dismissed after registering his or her candidacy and, if elected, may not be dismissed until one year after his or her term expires.

The Constitution introduced a number of significant labor reforms, such as a reduction in the workweek from 48 hours to 44 hours and a six-hour limit on the duration of an uninterrupted work shift. In addition, pregnant workers may not be dismissed for taking maternity leave of up to four months.

Unions in certain sectors of the economy, including the petroleum, metalworking and automobile industries, have staged strikes periodically primarily in an attempt to obtain higher wages. In May 1995, employees at Petrobrás, the largest corporation in Brazil, struck for approximately one month to obtain higher wages and in general opposition to the Government's privatization plans. Although labor actions have had some disruptive effects on certain industries, they have not impaired the implementation of *Plano Real* policies.

Social Security

In 1991, Congress enacted legislation to implement a state-operated social security and pension system. Employers are generally required to contribute 27.2% of each employee's wages to the system on a monthly basis (except for employers of domestic servants, who contribute 12% of wages), while employees generally contribute between 8% and 10% of their monthly wages for retirement benefits (paid in connection with retirements due to old age, illness or length of service), workers' compensation, death benefits, maternity leave, sick leave, disability and other social services. On August 1, 1995, the contribution of employees earning monthly wages between R$416.31 and R$836.90 was increased to 11.0%. The amount of most social security payments is primarily based upon the amount of monthly contributions made by the beneficiary. Social security payments prior to 1996 were indexed to the National Consumer Prices Index (INPC), and the amount of such payments was readjusted when the minimum wage was modified. The readjustment of social security payments is now based on the GPI-DS. In 1996 and 1997, social security payments increased 13.0% and 9.0%, respectively, in real terms. These benefits will be readjusted in subsequent years in the month of June.

In 1994, the Government proposed to reform the social security system in order to make it self-financing. This proposal required an amendment to the Constitution which was rejected by the Chamber of Deputies on March 6, 1996. On November 4, 1998, the Chamber of Deputies approved a version of the proposed amendment that replaces the current retirement system, which bases eligibility for benefits on length of service, with a system based upon a minimum retirement age, years of service and the amount of money the retiree contributed to the system. The minimum retirement ages are 48 for women and 53 for men (and 55 and 60, respectively, for new civil servants), provided they have made contributions to the retirement system for at least 30 and 35 years, respectively. In addition, notional individual accounts are to be established for participants of both the private retirement system (RGPS) and the public retirement system (RJU-Federal). The establishment of such individual accounts will require the passage of ordinary legislation. The Government has also proposed that the link between a retiree's accumulated contributions and expected pension be tightened. See "—Constitutional Reform—Social Security Reform".

Poverty and Income Distribution

Despite recent GDP growth, Brazil has experienced significant disparities in the distribution of wealth and income. Since 1960, the earliest date for which statistical information is available, the trend in income distribution in Brazil has been toward increasing inequality. According to the *Human Development Report 1996*, a United Nations survey, the per capita income of the poorest 20% in Brazil was $564 in 1993, while the average per capita income was $5,370. The study indicates that the disparity between average incomes of the richest 20% of the Brazilian population and the poorest 20% is high, with the richest 20% estimated to earn 32 times more than the poorest 20%. The study also estimates that 38% of the urban and 66% of the rural population of Brazil could be defined as poor, living on an income which is below the minimum amount needed to purchase essential food and non-food requirements.

As set forth in the table below, in 1996, 47.9% of the national income was concentrated in the hands of 10% of the economically active population. This income inequality manifests itself in regional disparities in social welfare. For example, according to the *Human Development Report 1994*, a United Nations survey, the northeastern region of Brazil lags behind the southern region in important social welfare indicators, with a 17-year disparity in life expectancy, a 33% disparity in adult literacy and a 40% disparity in real GDP per capita.

The following table outlines the data obtained from a 1996 survey on income distribution conducted by IBGE.

Table No. 14

Income Distribution of the Economically Active Population—1996

Income Group	% of National Income
Lowest 20%	3.4%
Next 20%	5.4
Next 20%	9.7
Next 20%	17.4
Highest 20%	64.1
Total	100.0%
Top 10%	47.9
Top 5%	34.1
Top 1%	13.5

Source: IBGE

A number of statistical measures suggest that the social welfare of lower-income groups in Brazil improved after the implementation of the *Plano Real*. For example, in 1995 and 1996 there were average increases of 33.5% and 8.3%, respectively, in the minimum wage, and recent research conducted by Seade Foundation and Dieese has indicated that the real income of the poorest 10% of the population increased by 18.2% in 1995 and 7.3% in 1996. Such figures suggest that lower rates of inflation have diminished the erosion of purchasing power, while renewed economic growth has led to wage increases. In addition, as measured by the São Paulo State Commerce Federation, food consumption in the metropolitan region of São Paulo increased by 26.4% in 1995 as compared to 1994 and by 2.5% in 1996. Much of this increase may be attributable to increased purchases by lower-income persons who, as a group, tend to spend a higher percentage of their income on food than higher-income persons.

The federal Government has established a Community Solidarity Program (*Programa Comunidade Solidária*) which provides educational support, food and vaccines to the poor. The program aims to promote partnerships between the federal Government and community organizations in addressing the needs of the poor not sufficiently met by other existing social welfare programs. Funding for the program is provided from a variety of federal sources, including the Government's general budget, FAT and the Severance Fund Contribution ("FGTS"). The program provides supplemental funding as a means to encourage the States to fund poverty programs in the poorest areas. Approximately 300 of the 1,702 municipalities considered by IBGE in 1995 to be the poorest communities in Brazil have been selected to receive priority status under the program. In 1995, the program oversaw disbursements of an aggregate of R$2.6 billion for nine community projects. In 1996 and 1997, approximately R$3.6 billion and R$2.9 billion, respectively, of federal funds were disbursed under this program to assist the poorest communities. The primary uses for such funds are to reduce infant mortality, provide supplemental aid to families in need and students and support education. In addition, State-based minimum income programs have been implemented in some cities such as Campinas and Ribeirão Preto in the State of São Paulo, and Brasília in the Federal District. These programs provide direct financial support to families with children of elementary school age and whose annual income is less than R$5,000. In 1997, the federal Government instituted the Minimum Income Guaranty Program, which grants financial support to minimum income programs operated by municipalities that lack sufficient resources to implement fully such programs. Such support will be limited to any municipality having per capita tax revenues (including constitutionally mandated revenue sharing transfers from the federal and State governments) and a per capita family income that are less than the averages for the State in which that municipality is located. Such support will also be limited to 50% of the total value of such municipal programs. The federal support is to be spent solely on families meeting the following criteria:

(i) per capita family income that is less than half of the minimum salary;

(ii) children or dependents under the age of 14; and

(iii) evidence of matriculation and attendance by all dependents between the ages of 7 and 14 at public schools or special education programs.

Environment

The Constitution contains a chapter on environmental protection, providing for the right to a clean environment and imposing upon the federal Government, the States, the Federal District and municipalities the duty to protect the environment, take measures against pollution and protect fauna and flora. In addition, legislation enacted in 1981 and 1985 provides that any individual or entity directly or indirectly causing environmental damage shall be held strictly liable and shall indemnify the damaged parties for any resulting losses. Various federal governmental agencies have the power to enforce environmental laws by imposing fines, ordering the shutdown of polluting facilities or denying or withholding tax and other benefits. Criminal sanctions, including imprisonment, may also be imposed upon violators. Despite constitutional and legislative protections for the environment, many areas of Brazil, and large urban areas in particular, suffer significant air, water and soil pollution.

Environmental problems in Brazil include industrial and urban pollution, deforestation and soil pollution and erosion arising from industrialization, rapid urbanization and rural poverty. In recent years, the federal Government has, through modern environmental legislation, established broad ambient quality standards, introduced procedures and requirements for environmental licenses, set aside areas for the preservation of critical ecosystems and intervened whenever State environmental agencies were not carrying out their responsibilities. In addition, federal, State and local government entities have, with the assistance of multilateral lenders such as the World Bank and the IDB, undertaken several projects in recent years that are intended to address existing environmental problems in certain large metropolitan areas.

Large-scale projects undertaken to build or improve water treatment facilities and to clean up water supplies that are heavily polluted with urban and industrial waste include a $793 million program to clean up Guanabara Bay in the State of Rio de Janeiro. Funded in part by a $350 million loan from the IDB and $294.2 million in cofinancing from the Overseas Economic Cooperation Fund of Japan, the program aims to improve sewage collection and treatment through the construction or expansion of sewage treatment plants, increase supplies of potable water, improve solid waste collection and disposal and monitor environmental conditions in the bay. Approximately 7.3 million persons live on the shores of the bay, which borders much of the Rio de Janeiro metropolitan region. The IDB also approved in September 1995 a $264 million loan to the State of Bahia to finance a $440 million program to expand waste collection and disposal services, install treatment plants and pumping facilities and build sanitary facilities for the municipalities surrounding the Todos os Santos Bay, an important tourist area with many sites of historical interest dating back to the colonial period.

Air pollution, an environmental problem in Brazil's largest cities, has also been the focus of certain recent environmental initiatives. In the municipality of São Paulo, where the large number of vehicles contributes to dangerously high levels of air pollution in the city during the winter, vehicle inspections have been tightened in an effort to reduce emissions by the buses and trucks that drive through the city. On May 1, 1995, the Secretary of the Environment for the State of São Paulo also launched a program to reduce traffic in the city. In the State of Paraná, the municipality of Curitiba has modernized its mass transit facilities in an effort to reduce vehicular traffic through the construction of new bus terminals and the acquisition of the largest buses in the world. The Curitiba improvements have been financed in part with a $120 million loan from the IDB.

The rapid growth of slums *(favelas)* in certain municipalities such as Rio de Janeiro and São Paulo has left many parts of such municipalities without adequate infrastructure. Many such *favelas* lack sewage systems and adequate storm drainage systems and often do not receive such city services as garbage collection and rodent control. In an effort to address such problems, the municipality of Rio de Janeiro is implementing a Favela-Bairro (Slum to Neighborhood) program, which is intended to improve the living conditions of the city's poor through, among other things, the paving of streets to permit garbage collection, the installation of water and sewage systems, reforestation and geological improvements to prevent flooding and landslides. The cost of this $300 million program is being funded in part through a $180 million loan by the IDB to the municipality of Rio de Janeiro. In July 1996, the IDB announced the approval of a $150 million loan to the municipality of São Paulo to support a similar program in that city.

In addition to the programs described above, there have been significant recent initiatives to conserve Brazil's threatened rain forest and biological diversity. Significant among these is the Pilot Program to Conserve the Brazilian Rain Forest, a G-7 initiative coordinated through the Rain Forest Trust Fund, a trust fund administered by the World Bank. The Brazilian Ministry of the Environment is also implementing a National Biodiversity Program, which is aimed at studying and protecting Brazil's biological diversity. Although Brazil occupies nearly half of South America and contains the world's largest standing tropical rain forest, the largest inland wetland, large expanses of semi-arid scrubland and vast tree and shrub woodlands, much of the country's biological diversity remains poorly understood. The National Biodiversity Program is to sponsor a series of workshops concerning each of Brazil's major biomes, as well as a small number of model subprojects designed to conserve biodiversity in certain specified areas. A biodiversity sinking fund would also be created to support additional conservation projects based on priorities established in the workshops. The National Biodiversity Program is estimated to cost in excess of $50 million and is to be partially financed through a $30 million grant from the World Bank's Global Environmental Trust. Other significant conservation projects include natural resource management projects in the State of Mato Grosso (a $286 million program funded in part through a $205 million loan from the World Bank) and the State of Rondônia (a $229 million program funded in part through a $167 million loan from the World Bank).

The Ministry of the Environment (*Ministério do Meio Ambiente, dos Recursos Hídricos e da Amazônia Legal*) is the federal body responsible for formulating and implementing environmental policies. The National Council on the Environment (CONAMA) prepares environmental regulations, and the Brazilian Institute of the Environment and Renewable Resources (IBAMA) is charged with supervising and overseeing the application of those regulations.

Education

According to a research study conducted by the Ministry of Education, there were 336,270 schools in Brazil in 1997, of which 37.3% were preschools, 58.0% were elementary schools, 4.4% were high schools, 0.3% were universities and 0.03% were postgraduate institutions. The total student enrollment in these schools amounted to 53,704,072, of which 12.2% were in preschool, 70.7% were in elementary school, 13.2% were in high school, 3.8% were in universities and 0.1% were in postgraduate institutions.

Federal Government expenditure on education in 1997 was approximately R$7.8 billion, of which 56.0% was used for higher education, 20.6% for elementary education, 5.8% for secondary education, 0.8% for preschool education and the remaining 16.8% for other programs. The amount budgeted for education (including culture) in 1998 was approximately R$12.0 billion. Effective January 1, 1998, the Government established a Fund for the Maintenance and Development of Basic Education and Teacher Training (*Fundo de Manutenção e Desenvolvimento do Ensino Fundamental e Valorização de Magistério* or "FUNDEF") pursuant to Constitutional Amendment No. 14 dated December 9, 1996, as regulated by Law No. 9,424 of 1996. FUNDEF, which is intended to increase overall funding for education, is to be funded through collections of the tax on circulation of goods and services (ICMS) and other taxes; 15% of such collections are to be allocated to FUNDEF.

The enrollment rate of children between the ages of 7 and 14 has increased steadily in the last years, reaching an estimated 96.1% in 1997, while the illiteracy rate of the population aged 15 and older has declined sharply from 39.7% in 1960 to an estimated 14.7% in 1997.

Competition Law

In June 1994, the Brazilian Congress enacted an antitrust law designed to promote free competition, to prevent excessive concentrations of economic power contrary to the public interest and to avoid excessive price increases. The law sets forth general criteria for determining anti-competitive behavior, such as tying, refusing to deal, price fixing, predatory pricing, exclusive dealing arrangements and resale price maintenance. The Government has used its new antitrust powers to supervise the marketplace in concentrated industries in an effort to prevent exaggerated price increases which could affect public confidence in the *Plano Real.*

In addition, the law requires that all documents relating to any merger, acquisition or asset sale that may limit or otherwise restrain open competition be filed within fifteen days of such transaction with the Economic Defense Secretariat (*Secretaria de Defesa Econômica or "SDE"*) of the Finance Ministry and the Administrative Council for Economic Defense (*Conselho Administrativo de Defesa Econômica* or "CADE") if such transaction would result in a 20% or greater market share for a company or group of companies or in which any of the participants has reported in its most recent balance sheets annual gross income equal to or greater than R$400 million. The SDE has the option of initiating administrative proceedings before the CADE to challenge any such transaction. In any administrative proceeding before it, the CADE has the power to impose fines or to grant equitable relief as well as to determine that the transaction be partially or totally reversed. In addition, a private party aggrieved by anticompetitive behavior has standing to sue in federal court on behalf of itself and similarly situated parties and may seek both equitable relief and monetary damages.

Patent Law

On May 14, 1996, President Cardoso signed Law No. 9,279 (the "Patent Law"), approving the new rules related to industrial property which comply with the basic guidelines of the Paris Convention for the Protection of Industrial Property and the Trade-Related Aspects of Intellectual Property Rights.

The Patent Law sets forth the rights and obligations pertaining to industrial property through (i) concessions of invention patents and working models, (ii) concessions of industrial design registrations, (iii) concessions of trademark registrations, (iv) the elimination of false geographic indications and (v) the curbing of unfair competition. Pharmaceutical products under development abroad and not in Brazil (known as *pipeline*) may also be registered and protected in Brazil.

The Patent Law also permits the registration of trademarks. Well-known trademarks are protected in their specific sector without the need for registration or filing in Brazil. If such recognized trademark has been registered in Brazil, however, such protection will be expanded to all activity sectors.

The Patent Law became effective May 15, 1997, except with regard to the provisions relating to *pipeline*, which took effect on May 15, 1996.

Law No. 9,609, which was enacted on February 19, 1998, extends copyright protection to computer software of a foreign entity, to the extent that the jurisdiction in which that foreign entity is located extends similar protections to Brazilian nationals. In addition, the new statute imposes penalties for copyright violations, including fines and prison sentences ranging from six months to four years.

BALANCE OF PAYMENTS AND FOREIGN TRADE

General

Brazil's balance of payments deteriorated at the end of the 1970s and in the early 1980s as a result in part of the rise in the price of petroleum, which at that time represented more than 40% of total imports, as well as rising U.S. dollar interest rates, which increased the cost of servicing Brazil's external debt. These developments led to current account deficits, the debt crisis and curtailment of Brazil's access to international financial markets. During that period, except for funds tied to debt rescheduling, the inflow of resources to Brazil was limited largely to traditional import financing and direct foreign investment and in amounts smaller than the debt service required for public sector external debt.

Since 1990, the Government's economic policies have increased the importance of the external sector of the economy. Recent reforms directly affecting the external sector include a reduction in import tariffs, the elimination of most non-tariff barriers, the negotiation of the Mercosul free trade agreement, the liberalization of certain foreign exchange transactions and the liberalization of foreign investment regulations. See "—Foreign Exchange Rates and Exchange Controls" and "The Brazilian Economy—Historical Background to Economic Policies".

From 1989 through 1994, Brazil maintained a surplus in its balance of payments. Although at the start of the period growth in net investment was relatively slow, increases in net investment have been larger since 1991. The result has been an increase in net foreign investment of 1,446% over the period. From December 31, 1989 through December 31, 1994, the foreign reserves maintained by the Central Bank increased 301%, totalling $38.8 billion at December 31, 1994.

Brazil's balance of payments remained strong in 1995 and 1996, registering surpluses of $13.0 billion and $8.7 billion, respectively. In October 1997, however, the Asian financial crisis led to a sell-off of Brazilian securities, adversely affecting Brazil's balance of payments for that year. The balance of payments registered a deficit of $7.9 billion in 1997, attributable in large part to net outflows related to portfolio divestment and to a continued erosion of Brazil's trade balance, which registered a deficit of approximately $6.8 billion. Although net investment increased substantially in 1998, Brazil's balance of payments deficit more than doubled to $17.3 billion that year. The increase in the deficit was attributable in part to an increase in net service expenditures and $33.7 billion in net outflows of short-term capital. See "—Balance of Payments".

In 1994, the net inflow of foreign investment decreased slightly to $13.5 billion from $13.7 billion in 1993, while net direct investment (excluding intercompany loans) increased to $2.0 billion, from $0.7 billion in 1993. In 1994, net portfolio investment decreased to $11.6 billion (excluding external debt restructuring bonds) from $13.0 billion in 1993, reflecting, in part, the effects of the Mexican liquidity crisis in late 1994. Concerns about potential currency devaluation led to a further net outflow of $3.7 billion of net portfolio investment in the first quarter of 1995. This situation was reversed in the second, third and fourth quarters of 1995, with net inflows of $3.7 billion, $7.1 billion and $3.0 billion, respectively, in portfolio investments. Total net inflows in 1995 reached $14.3 billion, a 5.9% increase over the $13.5 billion recorded in 1994. Total net inflows more than doubled in 1996, amounting to $31.8 billion. Net portfolio investment inflows reached $21.8 billion in 1996, a 117.9% increase over the amount of such inflows in 1995, and net direct investment inflows totalled $10.0 billion in 1996, a 130.1% increase from the previous year.

Foreign investment remained strong during the first nine months of 1997. Total net inflows during that period amounted to $27.8 billion, of which $16.1 billion represented net portfolio investments, and $11.7 billion represented net direct investments. A sell-off of Brazilian securities in late October 1997 and related declines in the Brazilian stock markets resulted in net portfolio outflows of approximately $7 billion during the last quarter of 1997. Brazil ended the year with total net foreign investment of $26.2 billion, a 17.5% decline from 1996. Of that amount, $9.1 billion represented net portfolio investments, and $17.1 billion represented net direct investments.

In August 1998, adverse developments in Russia led to another sell-off of Brazilian securities, as investors sought to reduce their exposure to emerging markets. Nevertheless, total net foreign investment increased 69.4% in 1998 to $44.4 billion. Net portfolio investment more than doubled in 1998 to $18.2 billion, but was still lower than the $21.8 billion recorded in 1996. Foreign direct investment inflows increased 53.0% in 1998, totaling $26.1 billion. Of that amount, 23.4%, or $6.1 billion, resulted from foreign participation in the national privatization program. In the first eight months of 1999, foreign direct investment inflows totalled $19.9 billion, bringing such investment to $30.6 billion in the twelve months ended August 31, 1999. See "—Foreign Investment".

Declines in foreign investment and concerns that the *real* might be overvalued contributed to a decrease in international reserves from $38.8 billion at December 31, 1994 to $31.9 billion at April 30, 1995. International reserves rose to approximately $51.8 billion at December 31, 1995 and reached $60.1 billion as of December 31, 1996 (corresponding to approximately 14 months of imports of goods). The Government used a portion of its international reserves to intervene in the foreign exchange markets following the sell-off of Brazilian securities in late October 1997 and related declines in the Brazilian stock markets, causing international reserves to fall to approximately $52.2 billion at December 31, 1997. International reserves recovered during the first four months of 1998, reaching a historical high of $74.7 billion at April 30, 1998. At July 31, 1998, Brazil's international reserves stood at approximately $70.2 billion, corresponding to approximately 14 months of imports of goods.

However, in August and September 1998, Brazil's international reserves came under pressure due to a significant sell-off of Brazilian securities. Although outflows in August 1998 were partially offset by net foreign direct investment, Brazil's international reserves declined to $67.3 billion at August 31, 1998, $45.8 billion at September 30, 1998 and $42.4 billion at October 31, 1998. Brazil negotiated a $41.8 billion IMF-led support package in November 1998 and received the first disbursement (in the amount of $9.3 billion) under that support package in December 1998. After giving effect to that disbursement, Brazil's international reserves stood at $44.6 billion on December 31, 1998. In January 1999, Brazil's international reserves came under significant pressure once again as a result of a series of events that month, including a failed attempt to effect a controlled devaluation of the *real* by widening the band within which the *real* was permitted to trade. The Central Bank subsequently announced that the *real* would be permitted to float, with Central Bank intervention to be made only in times of extreme volatility. After giving effect to a second disbursement (in the amount of $9.8 billion) under the IMF-led support package and a global offering of debt securities by Brazil, the Republic's international reserves stood at $33.8 billion at March 31, 1999. See "—International Reserves".

The Government frequently adjusts details of fiscal policy in order to promote or restrict the flow of foreign capital into Brazil. Measures taken by the Government for these purposes include: raising or lowering tax rates on financial transactions; establishing restrictions on investments in fixed income assets; authorizing or prohibiting settlement of foreign loans and financings in advance; and raising or lowering the net amount of foreign reserves a bank may hold without depositing such reserves in the Central Bank.

Balance of Payments

In 1992, 1993 and 1994, Brazil's balance of payments registered surpluses of $15.1 billion, $9.2 billion and $7.3 billion, respectively. However, in the first quarter of 1995, the balance of payments registered a deficit of $5.1 billion, attributable in part to concerns that the *real* was overvalued and to net outflows related to portfolio investment. These developments were, in turn, partially due to the Mexican financial crisis that took place in late 1994. The balance of payments deficit, however, was short-lived, and the third quarter of 1995 generated a $15.6 billion surplus. For the year ended December 31, 1995, the balance of payments registered a surplus of $13.0 billion. The favorable balance of payments continued in 1996, registering a surplus of $8.7 billion.

The Asian financial crisis led to a sell-off of Brazilian securities in late October 1997, adversely affecting Brazil's balance of payments in 1997. The balance of payments registered a deficit of $7.9 billion in 1997, attributable in large part to net outflows related to portfolio investment and to a continued erosion of Brazil's trade balance, which registered a deficit of approximately $6.8 billion.

Although net investment increased substantially in 1998, Brazil's balance of payments deficit more than doubled to $17.3 billion that year. The increase in the deficit was attributable in part to an increase in net service expenditures and $33.7 billion in net outflows of short-term capital.

After recording a $6.1 billion current account surplus in 1992, Brazil registered a $592 million current account deficit in 1993. Among the factors that led to that decline were reductions of 12.7% and 24.8% in the trade surplus and the net inflow of unilateral transfers, respectively, and an increase of 37.4% in the service deficit, reflecting an increase both in external debt service costs and expenses related to other services. In 1993, exports totalled $38.6 billion and imports totalled $25.3 billion. See "—Foreign Trade". Unilateral transfers, which include both gifts and migrant transfers, amounted to $2.2 billion in 1992 and $1.7 billion in 1993. In 1994, the current account registered a deficit of $1.7 billion due to a decrease of 21.3% in the trade surplus. The net outlays on services decreased 5.4%, while the net inflows in the form of unilateral transfers increased by 53.5%. The reduction in the trade surplus resulted from a 31.0% increase in imports, which totalled $33.1 billion, particularly in imports of consumer goods including passenger cars and capital goods which rose 73.0% and 49.0%, respectively, as a result of the *Plano Real.* Exports increased by 12.9% in 1994, totalling $43.5 billion. In 1995, the trade balance registered a deficit of $3.4 billion, reflecting increases of 50.7% in imports and 6.8% in exports in comparison with 1994, due mainly to the reduction of tariffs in the context of strong domestic demand for foreign products. The net expenditures on services totalled $18.6 billion while net inflows related to unrequited transfers reached $4.0 billion.

In 1996, the current account showed a deficit of $23.1 billion, mainly as a result of a $2.2 billion increase in the trade deficit and a $1.9 billion increase in the net service expenditures. Exports totalled $47.7 billion, a 2.7% increase in comparison with 1995, while imports totalled $53.3 billion, a 6.9% increase in comparison with 1995. Net service expenditures totalled $20.5 billion in 1996, a 10.2% increase in comparison to 1995. Unilateral transfers totalled $2.9 billion, representing a 27.0% decline compared to 1995.

Brazil's current account deficit continued to grow in 1997, reaching $30.9 billion at December 31, 1997. The increase in the current account deficit was largely attributable to a $1.3 billion increase in the trade deficit and a $5.8 billion increase in net service expenditures. Exports increased 11.0% to $53.0 billion, while imports rose 12.3% to $59.8 billion. Net service expenditures totalled $26.3 billion, a 28.3% increase over 1996. Unilateral transfers declined 23.6% to $2.2 billion.

The current account deficit increased 6.5% during the first six months of 1998 from the same period in 1997, largely as a result of a $709 million increase in net interest payments. However, developments in Russia in August 1998 put pressure on Brazil's current account balance. Although Brazil's trade deficit declined 3.7% to $6.6 billion in 1998, net capital inflows decreased 48.5% to $13.4 billion and net service expenditures increased 12.2% to $29.5 billion. Consequently, Brazil's current account registered a deficit of $34.3 billion in 1998.

At August 31, 1999, the current account deficit stood at $15.6 billion, the result of a $706 million trade deficit and $16.3 billion in debt service during the first eight months of 1999.

Brazil's capital account includes direct investments, portfolio investments and short-, medium- and long-term indebtedness. Net capital inflows amounted to $10.9 billion in 1993 compared to 1992, when the net capital inflows totalled $10.3 billion, including $9.5 billion in arrears refinanced with the Paris Club and $7.1 billion refinanced with banks (IDU bonds). In 1993, net inflows in the form of portfolio investments (including bonds, notes and commercial paper) totalled $13.0 billion. During the same period, there was a net inflow of short-term capital amounting to $1.5 billion, in comparison with a net outflow of $12.2 billion in 1992, principally as a result of a reduction of $14.3 billion in interest arrears in 1992. In 1994, there was a net outflow of short-term capital of $3.9 billion, primarily as a result of a refinancing of $6.4 billion of interest arrears in connection with the external debt restructuring. Net capital inflows in 1994 were reduced to $8.7 billion from $10.9 billion due in part to a decrease in net portfolio investment inflows, which totalled $11.6 billion in 1994 (excluding external debt restructuring bonds) as compared with $13.0 billion in 1993.

In 1995, net capital inflows totalled $28.8 billion primarily due to inflows of $17.3 billion in short-term capital, arising from foreign credit lines taken by banks to loan to export sector companies, as well as investments of foreign funds attracted by high-yielding short-term Brazilian debt instruments. In 1996, net capital inflows continued to grow, amounting to $34.0 billion. Net foreign direct investment increased sharply, reaching $10.0 billion, while net foreign portfolio investment amounted to $22.1 billion. Other short-term capital net inflows decreased to $5.2 billion in 1996 from $17.3 billion in 1995.

Net capital flows were adversely affected by the Asian financial crisis in 1997. The sell-off of Brazilian securities and related declines in the Brazilian stock markets resulted in net capital outflows in October 1997 of approximately $5 billion. Although capital inflows recovered during the last two months of 1997, net capital inflows totalled $26.0 billion in 1997, a 23.3% decline from 1996. Most affected by the Asian financial crisis were net foreign portfolio investment, which declined 58.6% to $9.1 billion, and other short-term capital net flows, which registered net outflows of $13.3 billion versus the $5.2 billion in net inflows recorded in 1996.

Net capital inflows amounted to $32.2 billion during the first half of 1998, a 116.7% increase over the same period in 1997. Significant net capital outflows occurred during the second half of 1998, however, reflecting concerns arising from adverse developments in Russia. Net capital inflows in 1998 totalled $13.4 billion, a 48.5% reduction from 1997. Net short-term capital outflows of $33.7 billion in 1998, reflecting the reduction of foreign trade financing and the withdrawal of foreign funds attracted by high-yielding short-term Brazilian debt instruments, were largely responsible for the reduction in net capital inflows that year. The reduction in net capital inflows was also attributable to an $8.6 billion (or 58.3%) reduction in net inflows of medium- and long-term capital; such net inflows totalled $6.1 billion in 1998. By contrast, net direct investment increased 46.5% in 1998 to $22.7 billion and net portfolio investment doubled to $18.2 billion.

The following table sets forth information regarding Brazil's balance of payments for each of the periods indicated.

Table No. 15

Balance of Payments(1)

	1994	1995	1996	1997(2)	1998(2)
			(in millions of dollars)		
Current Account	$ (1,689)	$ (17,972)	$ (23,137)	$ (30,916)	(34,296)
Trade Balance	10,466	(3,352)	(5,554)	(6,848)	(6,594)
Exports	43,545	46,506	47,747	52,990	51,120
Imports	33,079	49,858	53,301	59,838	57,714
Services (net)	(14,743)	(18,594)	(20,483)	(26,284)	(29,480)
Interest	(6,338)	(8,158)	(9,173)	(10,390)	(11,948)
Other	(8,405)	(10,436)	(11,310)	(15,894)	(17,532)
Unilateral Transfers(3)	2,588	3,974	2,900	2,216	1,778
Capital Account, Net	8,699	28,845	33,984	26,045	13,413
Direct Investments	934	2,753	10,032	15,515	22,735
Portfolio Investments(4)	54,051	10,322	22,060	9,141	18,243
Of which: 1994 Restructuring	42,476	311	249	—	—
Other Medium- and Long-Term Capital	(42,350)	(1,481)	(3,291)	14,723	6,137
Of which: Refinancing(5)	(39,410)	—	—	(449)	—
Other Short-Term Capital	(3,936)	17,251	5,183	(13,335)	(33,702)
Of which: Arrears(6)	(5,653)	(510)	(286)	—	—
Errors and Omissions	334	2,093	(2,109)	(3,002)	3,584
Surplus (Deficit)	7,344	12,966	8,738	(7,873)	(17,299)
Gold	(297)	(331)	342	247	(467)
SDRs	2	—	—	—	—
IMF Position	—	—	—	—	—
Foreign Exchange	(6,920)	(12,588)	(9,008)	7,660	8,437
Other Holdings	—	—	—	—	—
Use of IMF Credits(7)	(129)	(47)	(72)	(34)	4,789
Extraordinary Financing(8)	—	—	—	—	4,540

(1) These figures were calculated in accordance with the methodology set forth in the *IMF Balance of Payments Manual,* Fourth Edition.

(2) Preliminary.

(3) Unilateral transfers consist of transactions without a quid pro quo, many of which are gifts, and migrant transfers.

(4) Includes bonds, commercial paper and notes.

(5) The 1994 amount relates to transactions in connection with a Brady Plan-type restructuring completed that year. The 1997 amount relates to transactions in connection with the Republic's 1997 exchange offer. See "Public Debt—Debt Crisis and Restructuring—1992 Financing Plan".

(6) Represents mainly arrears on interest payments due but not paid on certain medium- and long-term bank indebtedness. The 1994 amount includes $6.4 billion in interest arrears in respect of certain external indebtedness restructured that year.

(7) In December 1998, the Republic received the first installment under a $41.8 billion IMF-led support package. See "The Brazilian Economy—*Plano Real* and Current Economic Policy".

(8) The 1998 amount consists of loans from the Bank for International Settlements and the Bank of Japan under the IMF-led support package. See "The Brazilian Economy—*Plano Real* and Current Economic Policy".

Source: Central Bank

Foreign Trade

Brazil's overall trade flows grew markedly in the four years ended December 31, 1997, rising from $76.6 billion in 1994 to $112.8 billion in 1997, a 47.2% increase. Much of the increase is attributable to the rise in imports; imports rose from $33.1 billion in 1994 to $59.8 billion in 1997, an 80.9% increase. During the same period, exports grew by 21.7%, from $43.5 billion in 1994 to $53.0 billion in 1997. As a result, the trade balance moved from a surplus of $10.5 billion in 1994 to a deficit of $6.8 billion in 1997. Because of a decline in economic activity in 1998, Brazil's overall trade flows declined to $108.8 billion that year. Imports declined by 3.5% to $57.7 billion in 1998, while exports declined by 3.5% to $51.1 billion that year. Brazil ended the year with a trade deficit of $6.6 billion.

During the first eight months of 1999, imports totalled $31.5 billion, a 15.6% reduction from the same period in 1998, while exports amounted to $30.8 billion, a 11.7% reduction from the same period in 1998. Brazil's trade deficit for the first eight months of 1999 was approximately $706 million.

Exports. Brazil's export mix has evolved significantly since the 1970s, with manufactured goods claiming an increasing share of total Brazilian exports. Manufactured goods comprised 15.2% of all Brazilian exports in 1970, growing to 44.8% in 1980, 54.1% in 1990 and 60.8% in 1993 before falling to 57.3% in 1994, 55.0% in 1995, 55.3% in 1996 and 55.1% in 1997. Manufactured goods comprised 57.5% of all Brazilian exports in 1998. At least part of the growth in exports of manufactured goods is attributable to increases in exports of higher value-added manufactured products.

Exports rose in each of the five years ended December 31, 1997, moving from $38.6 billion in 1993 to $43.5 billion in 1994, $46.5 billion in 1995, $47.7 billion in 1996 and $53.0 billion in 1997, increases of 7.7%, 12.9%, 6.8%, 2.7% and 11.0%, respectively, from the previous year. Exports, however, declined as a percentage of GDP, moving from 9.0% in 1993 to 8.0% in 1994, 6.6% in 1995, 6.2% in 1996 and 6.6% in 1997. Much of the export growth was fueled by increases in exports of food, beverage and tobacco products (which increased from $5.8 billion in 1993 to $8.6 billion in 1997, or 47.7%), vegetables, animals and animal products (which increased from $4.1 billion in 1993 to $8.0 billion in 1997, or 94.0%), machinery, appliances and electrical equipment (which increased from $4.6 billion in 1993 to $6.3 billion in 1997, or 36.0%), transportation equipment (which increased from $3.4 billion in 1993 to $5.6 billion in 1997, or 63.7%), and chemical products (which increased from $1.9 billion in 1993 to $3.0 billion in 1997, or 59.6%). Exports declined in 1998, dropping 3.5% to $51.1 billion or 6.6% of GDP.

The largest market for Brazilian products has been the European Union. In 1998, exports to the European Union amounted to approximately $14.7 billion, or 28.8% of all Brazilian exports. Exports to other Mercosul countries have risen from $2.3 billion in 1991, the year in which the Treaty of Asunción was signed, to $8.9 billion in 1998 and comprised 17.4% of all Brazilian exports in 1998, up from 7.3% in 1991. Exports to the United States also rose in 1998 to $9.9 billion, a 10.2% increase over the $9.0 billion in exports in 1994, and represented 19.3% of all Brazilian exports in 1998.

These trends have been influenced by Government initiatives to promote exports. The Government has maintained an export financing program, PROEX, which in 1991 replaced the predecessor FINEX program. In April 1997, PROEX was broadened to apply to both pre-shipment and post-shipment operations, and the list of eligible products thereunder, which was limited to certain capital goods, was extended to certain consumer products. The list of eligible products was further expanded on January 13, 1998, for purposes of both rate equalization and financing. In addition, on September 13, 1996, the Government approved the elimination of the State value-added tax ("ICMS") on exports of primary and semifinished goods and on the acquisition of certain fixed assets in an effort to liberalize the export sector and stimulate growth. The Government intends to reimburse States, for periods ranging from 6 to 10 years, for the loss of revenues resulting from the elimination of the ICMS. States experiencing revenue losses of up to 10% will be eligible for reimbursement for six years. The reimbursement period is extended by one year for each additional two percentage points of revenue losses above 10% up to a maximum reimbursement period of ten years. Aggregate reimbursement to the States totalled R$545.7 million in 1996, R$1.7 billion in 1997 and R$2.3 billion in 1998. The Government estimates that the aggregate reimbursement to the States will be R$3.5 billion for 1999 and subsequent years.

During 1996, the National Bank for Economic and Social Development (BNDES) also implemented certain changes to its export financing program, including the extension of credit lines to finance exports, and export credit insurance was re-established. The insurance provides coverage against certain commercial, political and extraordinary risks and is intended to encourage transactions with emerging market nations.

In 1997, the Government established two new funds to promote exports. The Export Guarantee Fund (*Fundo de Garantia à Exportação*) provides resources for covering the Government's guarantee of export credit insurance, and the Guarantee Fund for the Promotion of Competitiveness (*Fundo de Garantia para Promoção da Competitividade*) provides resources for covering the risk of financing operations conducted by BNDES and the Special Agency for the Financing of Machinery and Equipment (*Agência Especial de Financiamento de Máquinas e Equipamentos*, or FINAME). In addition, the Export Promotion Agency (*Agência de Promoção de Exportações*, or APEX) was created to support the implementation of export trade policy related to small businesses.

On September 9, 1998, the Government initiated the Special Export Program under the direction of the Foreign Chamber of Commerce (Camex). The Special Export Program covers 55 export sectors that accounted for almost 90% of Brazil's export revenues in 1997. The program is intended to foster export growth by, among other things, identifying obstacles to such growth.

Imports. After declining initially from $21.0 billion in 1991 to $20.6 billion in 1992, imports rose significantly in each of the five years ended December 31, 1997, moving from $25.3 billion in 1993 to $33.1 billion in 1994, $50.0 billion in 1995, $53.3 billion in 1996 and $59.8 billion in 1997, increases of 22.9%, 31.0%, 51.1%, 6.7% and 12.3%, respectively, from the previous year. Imports also grew as a percentage of GDP, moving from 5.9% in 1993 to 6.1% in 1994, 7.1% in 1995, 6.9% in 1996 and 7.4% in 1997. Much of the import growth was fueled by increases in imports of machinery and electrical equipment (which increased from $6.3 billion in 1993 to $19.2 billion in 1997, or 206.6%), chemical products (which increased from $3.4 billion in 1993 to $7.6 billion in 1997, or 121.5%), transportation equipment (which increased from $2.1 billion in 1993 to $6.4 billion in 1997, or 203.5%), and food products (which increased from $1.1 billion in 1993 to $3.3 billion in 1997, or 198.3%). The rapid growth in imports resulted in trade deficits of $3.5 billion in 1995, $5.6 billion in 1996 and $6.8 billion in 1997. Petroleum imports, which comprised 40.8% of all Brazilian imports in 1980, have declined as a percentage of total imports; such imports constituted 18.6% of all Brazilian imports in 1989, 7.1% in 1994, 5.2% in 1995, 6.5% in 1996, 5.2% in 1997 and 3.4% in 1998.

Because of a slowdown in economic activity, imports declined in 1998, dropping 3.5% to $57.7 billion, or 7.4% of GDP. Brazil ended 1998 with a trade deficit of $6.6 billion, a 3.7% decrease from the deficit registered the previous year.

Most of Brazil's imports come from the European Union, Brazil's largest trading partner. In 1998, imports from the European Union totalled $16.8 billion, or 29.2% of all Brazilian imports. An additional $13.7 billion in imports (23.7% of all Brazilian imports) came from the United States, and $9.4 billion (16.3% of all Brazilian imports) from the other members of Mercosul.

The significant growth in imports relative to exports in recent years was primarily attributable to the effects of reduced tariffs in the context of strong demand for foreign products. In 1991, the Government announced a schedule for tariff reductions for a three-year period ending in January 1994, aimed at attaining rates varying from 0% to 40%, with an average tariff of 14.2%. The Government subsequently accelerated certain scheduled adjustments and implemented the last set of tariff reductions on July 1, 1993, when the average duty and the maximum tariff were reduced to 14.4% and 40%, respectively. In an effort to contain inflation, the Government also implemented in September and October 1994 significant new tariff reductions, covering over 5,000 products and reducing the average tariff to 11.32%. As of November 30, 1997, the average tariff was 13.8%.

Average tariffs are also being reduced as a result of Brazil's implementation of a schedule of preferences applicable to imports from Mercosul countries. Mercosul members enjoyed a 75% discount from otherwise applicable rates during the second half of 1993 and 82% during the first half of 1994. This discount was raised to 89% beginning July 1, 1994 and to 100% beginning January 1, 1995, although certain products were excepted from this discount. In December 1994, the four member countries of Mercosul established January 1, 1995 as the date for the implementation of the CET, intended to transform the region into a customs union. The CET ranges from 0.0% to a maximum of 20.0%, but each member country was allowed a certain number of exceptions to the CET. The products on each country's list of exceptions have tariffs varying from the CET, but such tariffs are scheduled to be reduced automatically each year until 2001, at which time such tariffs will be equal to the CET rates.

In February 1995, the Minister of Finance increased the import tariff on passenger cars to 32.0% from 20.0%, with a scheduled reduction of 2.0 percentage points each year until 2001, when the tariff was to return to 20.0%. In addition, in order to reduce the current account deficit, in March 1995, the Minister of Finance increased to 70.0% the import tariff on roughly 100 durable consumer goods, including passenger cars (but not utility vehicles), home appliances and electric and electronic equipment, for a period of one year. In May 1995, the tariff on utility vehicles was also raised to 70.0%. In April 1995, tariffs on approximately 20 of such durable goods were reduced to a range between 40.0% and 63.0% to meet the tariff levels established in GATT negotiations. In December 1997, the Government changed the mechanism that permitted imports under special rates of machines and equipment of a type not manufactured in Brazil and established a 5% rate for capital goods, telecommunications and computer-related goods.

The Government imposes import quotas on certain products. In May 1996, quotas were imposed on textiles imported from China, Taiwan, South Korea, Panama and Hong Kong in accordance with World Trade Organization regulations that permit protection of important domestic industries which could be materially damaged because of imports. In addition, although quotas for vehicle imports were eliminated on October 26, 1995, tariffs remain high. Effective January 1, 1996, the import tax on passenger automobiles, light transport vehicles, motorcycles and bicycles was set at 70%. A discount of up to 50% of import duties on vehicles is available to production plants in Brazil and domestic producers. Moreover, in August 1996, a special tariff rate was established for one year for passenger automobile imports from Japan, the European Union and South Korea for an aggregate maximum of 50,000 vehicles (the quota to be allocated pro rata among such countries according to their respective import shares over the last three years). The rate was set at 50% of the normal tariff rate and was to have been in effect for one year. A decree issued in 1997 retained the special tariff rate for Japan, the European Union and South Korea and adjusted only the allocation of the quota among them. Imports by automobile manufacturers which have production plants in Brazil are not limited by the quota.

Brazil is a signatory to the Final Act of the GATT Uruguay Round, pursuant to which it has committed to staged reductions in tariffs beginning in 1995 over five years with respect to industrial products and over ten years with respect to agricultural products.

The following table sets forth certain details regarding Brazil's foreign trade for the years indicated:

Table No. 16

Principal Foreign Trade Indicators

	1994	1995	1996(1)	1997(1)	1998(1)
Exports as % of GDP	8.0%	6.6%	6.2%	6.6%	6.6%
Imports as % of GDP	6.1	7.1	6.9	7.4	7.4
Trade Balance as % of GDP	1.9	(0.5)	(0.7)	(0.9)	(0.8)
Growth (Decline) in foreign trade(2)	20.1	25.9	4.7	11.7	(3.5)
Exports—% Increase (Decrease)(3)	12.9	6.8	2.7	11.0	(3.5)
Imports—% Increase (Decrease)(3)	31.0	51.1	6.7	12.3	(3.5)
Trade balance—% change from prior period	(21.3)	(133.1)	(60.2)	(23.3)	(3.7)
Exports/Imports(4)	1.3	0.9	0.9	0.9	0.9
Exports					
$ in millions	$ 43,545	$ 46,506	$ 47,747	$ 52,990	$ 51,120
1,000 tons	195,294	200,792	199,332	208,857	230,124
% change from prior period(5)	6.9	2.8	(0.7)	4.8	10.2
Imports					
$ in millions	$ 33,079	$ 49,972	$ 53,301	$ 59,838	$ 57,714
1,000 tons	81,268	88,459	108,533	87,369	91,184
% change from prior period(5)	4.5	8.8	22.7	(19.5)	4.4
Trade Balance ($ in millions)	$ 10,466	$ (3,466)	$ (5,554)	$ (6,848)	$ (6,594)

(1) Preliminary.
(2) Percentage change in exports and imports from previous year.
(3) Percentage change from previous year.
(4) Exports divided by imports.
(5) Percentage change in volume, by weight.
Source: Central Bank

The following tables set forth certain information regarding exports and imports by major commodity groups for the periods indicated.

Table No. 17

Exports (FOB Brazil) by Major Commodity Groups

	1994		1995		1996		1997		1998	
Item	in $ millions	% of total	in $ millions	% of total	in $ millions	% of total	in $ millions	% of total	in $ millions	% of total
Vegetable, Animals and Animal Products	$ 6,197	14.2%	$ 5,683	12.2%	$ 5,643	11.8%	$ 8,007	15.1%	$ 7,477	14.6%
Food, Beverage and Tobacco	6,621	15.2	7,835	16.8	8,855	18.5	8,587	16.2	7,839	15.3
Mineral Products	3,423	7.9	3,297	7.1	3,502	7.3	3,550	6.7	4,012	7.9
Chemical Products	2,054	4.7	2,539	5.5	2,757	5.8	2,998	5.7	2,937	5.7
Rubber and Plastics	1,389	3.2	1,504	3.2	1,459	3.1	1,605	3.0	1,480	2.9
Leather and Shoes	2,141	4.9	2,130	4.6	2,394	5.0	2,407	4.5	2,128	4.2
Wood and Furniture	1,607	2.5	1,138	2.4	1,112	2.3	1,220	2.3	1,128	2.2
Paper and Paper Products	974	2.2	1,256	2.7	958	2.0	997	1.9	963	1.9
Textiles and Clothing	1,404	3.2	1,441	3.1	1,292	2.7	1,267	2.4	1,113	2.2
Metals	6,348	14.6	6,863	14.8	6,532	13.7	6,346	12.0	5,713	11.2
Machinery, Appliances and Electrical Equipment	5,136	11.8	5,478	11.8	5,764	12.1	6,314	11.9	6,051	11.8
Transportation Equipment	3,806	8.7	3,336	7.2	3,721	7.8	5,620	10.6	6,457	12.6
Other	2,985	6.9	4,008	8.6	3,765	7.9	4,073	7.7	3,822	7.5
Total	$43,545	100.0	$46,506	100.0	$47,747	100.0	$52,990	100.0	$51,990	100.0

Sources: Central Bank and Ministry of Industry, Commerce and Tourism

Table No. 18

Imports (FOB Country of Origin) by Major Commodity Groups

Item	1994 in $ millions	1994 % of total	1995 in $ millions	1995 % of total	1996 in $ millions	1996 % of total	1997 in $ millions	1997 % of total	1998 in $ millions	1998 % of total
Food	$ 2,014	6.1%	$ 3,514	7.0%	$ 3,263	6.1%	$ 3,251	5.4%	$ 3,052	5.3%
Clothing	487	1.5	988	2.0	1,021	1.9	1,141	1.9	935	1.6
Precision Instruments	1,141	3.5	1,836	3.7	2,132	4.0	2,223	3.7	2,254	3.9
Cereals	1,408	4.3	1,665	3.3	2,103	3.9	1,579	2.6	1,940	3.4
Fertilizers	634	1.9	661	1.3	859	1.6	951	1.6	977	1.7
Chemical Products	4,514	13.6	6,489	13.0	6,887	12.9	7,609	12.7	7,952	13.8
Wood Products, Cellulose & Derived Products	559	1.7	1,371	2.8	1,370	2.6	1,437	2.4	1,415	2.5
Rubber and Plastic Products	1,334	4.0	2,410	4.8	2,515	4.7	2,696	4.5	2,728	4.7
Steel and Cast Iron	432	1.3	699	1.4	794	1.5	1,226	2.0	1,362	2.4
Non-ferrous Metals	571	1.7	1,096	2.2	938	1.8	1,115	1.9	1,084	1.9
Fuel and Lubricants	4,766	14.4	5,581	11.2	6,911	13.0	6,783	11.3	5,148	8.9
Transportation Equipment	3,396	10.3	5,935	12.0	4,510	8.5	6,382	10.7	6,753	11.7
Machinery and Electrical Equipment	9,294	28.1	13,956	27.9	15,689	29.4	19,212	32.1	18,482	32.1
Other	2,529	7.6	3,772	7.5	4,308	8.1	4,234	7.1	3,468	6.0
Total	$33,079	100.0	$49,972	100.0	$53,301	100.0	$59,838	100.0	$57,550	100.0

Sources: Central Bank and Ministry of Finance

The following tables set forth certain information regarding the destination of Brazil's exports and the sources of its imports for the periods indicated.

Table No. 19

Exports (FOB Brazil) by Region

Item	1994 in $millions	1994 % of total	1995 in $millions	1995 % of total	1996 in $millions	1996 % of total	1997 in $millions	1997 % of total	1998 in $millions	1998 % of total
EFTA(1)	$ 382	0.9%	$ 505	1.1%	$ 503	1.1%	$ 378	0.7%	$ 360	0.7
LAIA(2)	9,464	21.7	9,494	20.4	10,474	21.9	12,831	24.2	12,618	24.7
Canada	501	1.2	461	1.0	506	1.1	584	1.1	544	1.1
EEC(3)	12,202	28.0	12,912	27.8	12,836	26.9	14,513	27.4	14,744	28.8
Eastern Europe	534	1.2	985	2.1	1,056	2.2	1,313	2.5	1,163	2.3
USA(4)	8,951	20.5	8,798	18.9	9,312	19.5	9,407	17.8	9,865	19.3
Japan	2,574	5.9	3,102	6.7	3,047	6.4	3,068	5.8	2,202	4.3
OPEC(5)	1,465	3.4	2,036	4.4	2,231	4.7	2,651	5.0	2,749	5.4
Other	7,472	17.2	8,213	17.7	7,782	16.3	8,245	15.6	6,875	13.4
Total excluding OPEC	$42,080	96.6%	$44,470	95.6%	$45,516	95.3%	$50,339	95.0%	$48,371	94.6%
Total	$43,545	100.0%	$46,506	100.0%	$47,747	100.0%	$52,990	100.0%	$51,120	100.0%
Mercosul	$ 5,922	13.6%	$ 6,154	13.2%	$ 7,305	15.3%	$ 9,044	17.1%	$ 8,877	17.4
Argentina	4,136	9.5	4,041	8.7	5,170	10.8	6,7[illegible]7	12.8	6,747	13.2
Paraguay	1,054	2.4	1,301	2.8	1,325	2.8	1,406	2.7	1,249	2.4
Uruguay	732	1.6	812	1.7	811	1.7	870	1.6	881	1.7

(1) European Free Trade Association. These figures have been adjusted to reflect the inclusion of Austria, Finland and Sweden in the European Union.
(2) Latin American Integration Association; excludes Venezuela for the entire period.
(3) European Economic Community, now the European Union.
(4) Includes Puerto Rico.
(5) Organization of Petroleum Exporting Countries, including Venezuela.
Sources: Central Bank and Ministry of Industry, Commerce and Tourism

Table No. 20

Imports (FOB Country of Origin) by Region

Item	1994 in $millions	1994 % of total	1995 in $millions	1995 % of total	1996 in $millions	1996 % of total	1997 in $millions	1997 % of total	1998 in $millions	1998 % of total
EFTA(1)	$ 658	2.0%	$ 955	1.9%	$ 1,028	1.9%	$ 1,120	1.9%	$ 1,150	2.0%
LAIA(2)	5,776	17.5	9,142	18.3	10,613	19.9	13,113	21.9	12,363	21.4
Canada	835	2.5	1,128	2.3	1,258	2.4	1,416	2.4	1,338	2.3
EEC(3)	8,972	27.1	13,798	27.6	14,120	26.5	15,874	26.5	16,833	29.2
Eastern Europe	810	2.4	1,044	2.1	977	1.8	838	1.4	810	1.4
USA(4)	6,787	20.5	10,530	21.1	11,865	22.3	13,901	23.2	13,688	23.7
Japan	2,412	7.3	3,298	6.6	2,761	5.2	3,534	5.9	3,274	5.7
OPEC(5)	3,296	10.0	3,330	6.7	3,960	7.4	4,076	6.8	3,151	5.5
Other	3,533	10.7	6,748	13.5	6,719	12.6	5,966	10.0	5,107	8.8
Total excluding OPEC	$29,783	90.0%	$46,642	93.3%	$49,341	92.6%	$55,762	93.2%	$54,563	94.5
Total	$33,079	100.0%	$49,972	100.0%	$53,301	100.0%	$59,838	100.0%	$57,714	100.0%
Mercosul	$ 4,583	13.9%	$ 6,839	13.7%	$ 8,267	15.5%	$ 9,517	15.9%	9,427	16.3
Argentina	3,662	11.1	5,588	11.2	6,784	12.7	8,032	13.4	8,034	13.9
Paraguay	352	1.1	515	1.0	551	1.0	518	0.9	351	0.6
Uruguay	569	1.7	737	1.5	932	1.7	967	1.6	1,042	1.8

(1) European Free Trade Association. These figures have been adjusted to reflect the inclusion of Austria, Finland and Sweden in the European Union.
(2) Latin American Integration Association; excludes Venezuela for the entire period.
(3) European Economic Community, now the European Union.
(4) Includes Puerto Rico.
(5) Organization of Petroleum Exporting Countries, including Venezuela.
Sources: Central Bank and Ministry of Finance
NOTE: Imports are categorized according to the country of origin and not from the country where the product was acquired.

Foreign Investment

Foreign investment in Brazil has traditionally focused on direct investment in the manufacturing sector. Beginning in 1991, however, foreign investment rose substantially, surpassing the levels reached during the period from 1973 to 1982 (before the debt crisis), with much of the increase occurring in portfolio investments. Net inflows from foreign investments in 1991 totalled approximately $4.8 billion, a 223.2% increase over the previous year. In 1991, net portfolio investment and net direct investment amounted to $3.8 billion and $972 million, respectively, representing increases of 557.7% and 8.0%, respectively, over the previous year.

In 1992 and 1993, partly in response to changes in Brazil's foreign investment laws, net foreign investment continued to increase, rising to $8.9 billion and $13.7 billion, respectively. Much of the increase was attributable to growth in net portfolio investment, which rose 93.4% in 1992 to $7.4 billion and 75.8% in 1993 to $13.0 billion. Net direct investment, by contrast, increased 62.6% to $1.6 billion in 1992 but fell 54.8% to $714 million in 1993.

In 1994, the year in which Brazil completed its Brady Plan-type restructuring (see "Public Debt—Debt Crisis and Restructuring"), net inflows from foreign investments in 1994 declined slightly to $13.5 billion. Net portfolio investment (excluding bonds issued in Brazil's Brady Plan-type restructuring) dropped 10.6% to $11.6 billion in 1994 reflecting in part the effects of the Mexican liquidity crisis in December 1994, while net direct investment (excluding intercompany loans) increased 176.1% to $2.0 billion.

Concerns about potential currency devaluation led to a further net outflow of $3.7 billion of portfolio investments in the first quarter of 1995. This situation was reversed in the second, third and fourth quarters of 1995, with net inflows of $3.7 billion, $7.1 billion and $3.0 billion, respectively, in portfolio investments. Total net foreign investment in 1995 reached $14.3 billion, a 5.9% increase over the $13.5 billion recorded in 1994. Total net foreign investment more than doubled in 1996, amounting to $31.8 billion. Net portfolio investment inflows reached $21.8 billion in 1996, a 117.9% increase over the amount of such inflows in 1995, and net direct investment inflows totalled $10.0 billion in 1996, a 130.1% increase from the previous year.

Foreign investment remained strong during the first nine months of 1997. Total net inflows during that period amounted to $27.8 billion, of which $16.1 billion represented net portfolio investments, and $11.7 billion represented net direct investments. A sell-off of Brazilian securities in late October 1997 and related declines in the Brazilian stock markets resulted in net portfolio outflows of approximately $7 billion in the last quarter of 1997. Brazil ended the year with total net foreign investment of $26.2 billion, a 17.5% decline from 1996. Net foreign direct investment reached $17.1 billion, a 71.3% increase over 1996. However, net foreign portfolio investments declined 58.1% to $9.1 billion in 1997, largely as a result of net bond amortization in an aggregate amount of $4.9 billion in and a reduction to $9.0 billion from $14.7 billion in aggregate net inflows from note placements abroad.

In August 1998, adverse developments in Russia led to another sell-off of Brazilian securities, as investors sought to reduce their exposure to emerging markets. Nevertheless, total net foreign investment increased 69.2% in 1998 to $44.4 billion. Net portfolio investment almost doubled in 1998 to $18.2 billion, but was still lower than the $21.8 billion recorded in 1996. Foreign direct investment inflows increased 53.0% in 1998, totaling $26.1 billion. Of that amount, 23.4%, or $6.1 billion, resulted from foreign participation in the national privatization program. In the first eight months of 1999, foreign direct investment inflows totalled $19.9 billion, bringing such investment to $30.6 billion in the twelve months ended August 31, 1999.

The following table sets forth information regarding foreign investment in Brazil for each of the years indicated.

Table No. 21

Foreign Investment in Brazil

	Inflows			Outflows			Net Inflows		
	Portfolio(1)	Direct(2)	Total	Portfolio(1)	Direct(2)	Total	Portfolio	Direct	Total
				(in millions of dollars)					
1994	32,621	2,589	35,210	21,046	618	21,664	11,575	1,971	13,546
1995	35,857	5,476	41,333	25,846	1,163	27,009	10,011	4,313	14,324
1996	45,235	10,496	55,731	23,424	520	23,945	21,811	9,976	31,787
1997(3)	58,210	18,745	76,955	49,068	1,660	50,729	9,141	17,085	26,226
1998(3)	58,847	28,742	87,589	40,603	2,609	43,212	18,243	26,133	44,377

(1) Includes equity securities, bonds, commercial paper and notes, except those related to external debt restructuring bonds.
(2) Includes reinvested earnings and excludes intercompany loans.
(3) Preliminary.
Source: Central Bank

The following table sets forth information on net direct foreign investments by activity as of December 31, 1995, 1996 and 1997.

Table No. 22

Direct Investments by Activity(1)

	1995(2)		1996(3)		1997(3)	
	Value	%	Value	%	Value	%
			(in millions of dollars)			
Agriculture, cattle breeding, and mineral extraction	**$ 688.6**	**1.62%**	**$ 110.5**	**1.44%**	**$ 456.1**	**2.98%**
Agriculture, cattle breeding, and related services	207.2	0.49	37.9	0.49	0.0	0.00
Silviculture, forest exploitation and related services	30.5	0.07	0.0	0.00	108.5	0.71
Fishing, aquiculture and related services	7.9	0.02	0.0	0.00	0.0	0.00
Petroleum extraction and related services	72.0	0.17	46.8	0.61	10.0	0.07
Extraction of ores	330.3	0.78	25.8	0.34	337.6	2.20
Extraction of non-metallic ores	40.7	0.10	0.0	0.00	0.0	0.0
Manufacturing	**$23,402.4**	**55.03%**	**$1,740.0**	**22.70%**	**$ 2,036.4**	**13.30%**
Manufacture of food and beverages	2,332.4	5.48	185.9	2.43	322.9	2.11
Manufacture of tobacco products	715.4	1.68	250.0	3.26	0.0	0.00
Manufacture of textiles	527.8	1.24	72.8	0.95	50.2	0.33
Making of garments and accessories	78.1	0.18	0.0	0.00	10.0	0.07
Preparation of leather and production of leather articles and shoes	426.9	1.00	0.0	0.00	0.0	0.00
Manufacture of wood products	29.0	0.07	0.0	0.00	88.1	0.58
Manufacture of cellulose, paper and paper products	1,401.6	3.30	21.9	0.29	0.0	0.00
Publishing, printing and reproduction of recordings	116.6	0.27	0.0	0.00	11.8	0.08
Production of coke, petroleum, nuclear fuels and alcohol	0.0	0.00	0.0	0.00	11.0	0.07
Manufacture of chemical products	4,747.7	11.16	221.6	2.89	368.2	2.40
Manufacture of rubber and plastic articles	1,317.9	3.10	30.2	0.39	139.1	0.91
Manufacture of non-metallic products	816.1	1.92	194.9	2.54	207.7	1.36
Basic metallurgy	2,566.2	6.03	30.2	0.39	0.0	0.00
Manufacture of metal products	572.8	1.35	63.7	0.83	0.0	0.00
Manufacture of machines and equipment	2,072.3	4.87	179.2	2.34	206.6	1.35
Manufacture of office machines and data processing equipment	441.4	1.04	10.0	0.13	20.0	0.13
Manufacture of electrical machines, apparatus and materials	1,100.3	2.59	30.2	0.39	138.1	0.90
Manufacture of electronic materials and communication apparatus	589.7	1.39	62.1	0.81	185.6	1.21
Manufacture of medical, optical, automation equipment, time apparatus	168.4	0.40	57.8	0.75	11.0	0.07
Manufacture and assembly of motor vehicles trailers, vehicle bodies	2,851.3	6.70	286.1	3.73	222.7	1.45
Manufacture of other transportation equipment	223.0	0.52	0.0	0.00	0.0	0.00
Manufacture of furniture and other industries	294.4	0.69	43.4	0.57	43.4	0.28
Recycling	13.3	0.03	0.0	0.00	0.0	0.00
Services	**$18,439.0**	**43.36%**	**$5,814.9**	**75.86%**	**$12,818.6**	**83.72%**
Electricity, gas and hot water	0.2	0.00	1,626.4	21.22	3,554.4	23.21
Collection, treatment and distribution of water	1.8	0.00	0.0	0.00	0.0	0.00
Construction	202.7	0.48	0.0	0.00	53.1	0.35
Commerce and repair of motor vehicles; retail sale of fuels	83.4	0.20	16.3	0.21	176.9	1.16
Wholesale and commerce intermediation	2,104.8	4.95	207.0	2.70	690.6	4.51
Retail and repair of articles	667.6	1.57	406.0	5.30	84.9	0.55
Accommodation and catering	364.3	0.86	35.9	0.47	0.0	0.00
Land transportation	6.4	0.02	208.2	2.72	0.0	0.00
Water transportation	90.5	0.21	0.0	0.00	0.0	0.00
Air transportation	24.7	0.06	0.0	0.00	0.0	0.00
Transportation ancillary activities and travel agencies	71.4	0.17	0.0	0.00	0.0	0.00
Mail and communication	195.1	0.46	611.2	7.97	831.3	5.43
Financial intermediation	1,254.8	2.95	379.5	4.95	1,596.2	10.43
Insurance and private pension plan	149.0	0.35	148.3	1.93	191.0	1.25
Financial intermediation ancillary activities	113.8	0.27	36.1	0.47	60.0	0.39

	1995(2)		1996(3)		1997(3)	
	Value	%	Value	%	Value	%
			(in millions of dollars)			
Real estate activities	$ 1,057.4	2.49%	$ 82.9	1.08%	$ 40.4	0.26%
Rental of vehicles, machines, equipment and personal and household articles	363.3	0.85	16.7	0.22	35.2	0.23
Data processing and related activities	115.1	0.27	10.8	0.14	124.7	0.81
Research and development	5.5	0.01	0.0	0.00	0.0	0.00
Services rendered to companies	11,454.9	26.93	2,015.9	26.30	5,350.8	34.95
Education	1.1	0.00	0.0	0.00	0.0	0.00
Health and social services	17.8	0.04	0.0	0.00	0.0	0.00
Urban cleaning, sewers and related activities	2.2	0.01	0.0	0.00	0.0	0.00
Associative activities	54.4	0.13	13.7	0.18	0.0	0.00
Recreational, cultural and sport activities	14.5	0.03	0.0	0.00	29.1	0.19
Personal services	19.0	0.04	0.0	0.00	0.0	0.00
International organizations	3.3	0.01	0.0	0.00	0.0	0.00
Total	**$42,530.0**	**100.00%**	**$7,665.4**	**100.00%**	**$15,311.1**	**100.00%**

(1) Investments of more than $10 million.
(2) Census data as of December 31, 1995.
(3) Based on data from Certificates of Registration of foreign capital issued by the Central Bank of Brazil.
Source: Central Bank

The United States is the major source of foreign investment in Brazil. As of December 31, 1995, the United States provided 25.5% of all direct foreign investment in Brazil, followed by Germany (13.7%), Switzerland (6.6%), Japan (6.3%), France (4.8%), Canada (4.3%) and United Kingdom (4.2%). Total foreign direct investment (excluding intercompany loans) registered with the Central Bank as of that date was approximately $42.5 billion.

The Government has periodically taken measures to control the inflow of foreign capital in order to facilitate the conduct of monetary policy and to regulate the level of Brazil's international reserves. In 1993 and 1994, such measures were intended to reduce the inflow of private capital attracted by high interest rates in Brazil and included (i) an increase in the average minimum term of tax-exempt external loans (including Eurobonds and other fixed- or floating-rate obligations) to eight from five years, (ii) a measure prohibiting exporters from receiving payments more than six months prior to shipment, (iii) increases in taxes on certain types of foreign investments (including the IOF, a tax introduced in March 1994 and imposed on foreign investments in Brazilian stock exchanges), (iv) the imposition of a 15% reserve requirement on internal credits relating to advances on foreign exchange contract operations transfers, (v) the authorization of Brazilian companies to enter into forward liquidation contracts for foreign exchange and (vi) the suspension of inflows of foreign capital in the form of long-term advance export payments. The liquidity crisis in Mexico beginning at the end of December 1994 and the subsequent deterioration of Brazil's current account led the Government to reverse certain of such measures and to take others to reduce domestic consumption and stem the decline in international reserves. During that period, the Government, among other things, (i) eliminated the 15% reserve requirement relating to advances on foreign exchange contract operations and reduced the reserve requirement with respect to foreign exchange held by banks, (ii) limited advance payments on short-term import financings to 20% of the value of the imported merchandise, (iii) reduced the minimum term for internal relending of borrowed funds entering the country under Resolution No. 63 dated August 21, 1967 of the National Monetary Council ("Resolution No. 63") to 90 from 540 days and (iv) reduced the IOF tax on loans, investments in foreign capital fixed-income funds and portfolio investments. With the strong rate of growth in international reserves in July and early August 1995, the Government reimposed measures intended to restrict the inflow of foreign capital. The measures were bolstered by other initiatives in September and December 1995, which, among other things, gradually reduced the IOF tax rate on medium-term foreign currency loans, eliminated the discount applied to certain securities and foreign loans when tendered as consideration in the privatization program and eliminated taxes on income from direct foreign investment and reduced taxes on capital gains from such investments from 25% to 15%.

On February 8, 1996, the Government adopted several measures intended to direct inflows of foreign capital toward investments that promoted the Government's monetary policy objectives. Under the new measures, foreign capital subject to regulation under Resolution No. 1,289 dated March 20, 1987 of the National Monetary Council is no longer permitted to be invested in certain instruments having fixed yields, such as Agrarian Debt Bonds (TDA), Obligations of the National Fund for Development (OFND) and debentures issued by *Siderurgia Brasileira S.A.* (Siderbrás). Instead, longer term investments in loans having greater maturities and certain investment funds were encouraged through the imposition of IOF at a rate which declined with the duration of the loan or investment. Amounts made available to Brazilian banks for relending under Resolution No. 63 which are not so reloaned are no longer permitted to be invested in National Treasury Notes, series D (NTN-D) for borrowings authorized after February 8, 1996. In addition, those amounts not reloaned or not used for interbank on lending leasing transactions and acquisition of credit rights, pursuant to Circular No. 2,670 of March 1996, are required to be deposited in the Central Bank without any interest payable to the Brazilian bank.

On March 26, 1998, the National Monetary Council of Brazil adopted measures to control short-term inflows of foreign capital. Under the new rules, a maximum of 50% from external funds borrowed by banks to make loans to the agricultural sector, entering the country under Resolution No. 2,843 dated March 26, 1998 of the National Monetary Council, may be applied for investments in U.S. dollar-indexed National Treasury Notes.

In order to promote foreign investment, on April 25, 1997, the Government announced revised rates for the IOF. The revised rates included (i) a 0% rate on foreign currency transactions relating to loans and issuances of debt securities, and investments in non-fixed income securities and privatization funds and (ii) a 2% rate on foreign currency transactions related to investments in fixed income investment funds, interbank transactions with institutions abroad and inflows of short-term funds from non-residents of Brazil. After increasing IOF rates in December 1998, the Government again reduced such rates to 0% for the transactions described in clause (i) and 0.5% for the transactions described in clause (ii). The IOF may be increased to up to 25.0% under existing legal authority.

Foreign investment in non-voting shares of Brazilian financial institutions was authorized in December 1996. The issuance abroad of depositary receipts representing interests in such shares was also authorized.

International Reserves

During the four years ended December 31, 1996, Brazil substantially increased its total international reserves, and in particular its foreign exchange holdings, which are primarily denominated in U.S. dollars. During that period, international reserves increased by 153.1%.

The Mexican liquidity crisis that began in late 1994 contributed to an outflow of foreign capital from Brazil and a decline in international reserves in early 1995. See "—Foreign Investment". For this reason, and because the Central Bank used international reserves to stabilize the *real*-dollar exchange rate, foreign reserves declined to $33.7 billion at March 31, 1995 from $38.8 billion at December 31, 1994 and to $31.9 billion on April 30, 1995. International reserves generally rose thereafter reaching $60.1 billion on December 31, 1996 (corresponding to approximately 14 months of imports of goods), reflecting strong net foreign capital inflows during the period. The Government used a portion of its international reserves to intervene in the foreign exchange markets following the sell-off of Brazilian securities in late October 1997 and related declines in the Brazilian stock markets, causing international reserves to fall to approximately $52.2 billion at December 31, 1997. International reserves recovered during the first four months of 1998, reaching a historical high of $74.7 billion at April 30, 1998. At July 31, 1998, Brazil's international reserves stood at approximately $70.2 billion, corresponding to approximately 14 months of imports of goods.

However, in August and September 1998, international reserves came under pressure due to a significant sell-off of Brazilian securities. The Government believes that the sell-off was, in part, the result of inventors' decisions to reduce their exposure to emerging markets after expectations regarding emerging markets, in general, changed based on adverse developments in Russia. Although outflows in August 1998 were partially offset by net foreign direct investment, principally resulting from the privatization of Telecomunicações Brasileiras S.A., Brazil's international reserves declined to $67.3 billion at August 31, 1998, $45.8 billion at September 30, 1998 and $42.4 billion at October 31, 1988.

Brazil's international reserves stabilized following the announcement of a $41.8 billion IMF-led support package on November 13, 1998, reaching $41.2 billion at November 30, 1998. See "The Brazilian Economy—*Plano Real* and Current Economic Policy". The Central Bank also lowered the TBAN rate during this time from 49.75% to 42.25% on November 12, 1998 and 36% on December 17, 1998. In December 1998, however, there were significant outflows following the Government's failure to secure passage of a key social security reform bill by the Chamber of Deputies in a December 3, 1998 vote and delays in the voting of the increase of the CPMF rate. After giving effect to such outflows and the $9.3 billion initial aggregate disbursements under the IMF-led support package, reserves stood at $44.6 billion at December 31, 1998.

In January 1999, Brazil's international reserves came under significant pressure once again as a result of a series of events that month. On January 6, 1999, the newly inaugurated governor of the State of Minas Gerais announced that the State would suspend for 90 days payments in respect of the State's approximately R$18.3 billion debt to the Government. A week later, on January 13, 1999, Gustavo H.B. Franco, the president of the Central Bank and one of the architects of the *Plano Real*, resigned and was replaced by Francisco Lopes, who attempted a controlled devaluation of the *real* by widening the band within which the *real* was permitted to trade. Subsequent Central Bank intervention failed to keep the *real*-U.S. dollar exchange rate within the new band, however, and on January 15, 1999, the Central Bank announced that the *real* would be permitted to float, with Central Bank intervention to be made only in times of extreme volatility. Following that announcement, the value of the *real* against the U.S. dollar declined approximately 21% from its level on January 12, 1999.

To minimize excessive exchange rate volatility and reduce the inflationary effects of the devaluation of the *real*, the Central Bank raised its assistance rate (TBAN) to 41% from 36% on January 19, 1999, and the Central Bank intervened in the market to adjust the Federal Funds Rate (*taxa Over/Selic*) to 32% on January 19, 1999 from 29.8% the previous day. The *Over/Selic* rate was further increased to 35.5% on January 28, 1999 and 37.0% on January 29, 1999. Both the level of international reserves and the value of the *real* continued to decline, however; as of January 31, 1999, Brazil's international reserves stood at $36.1 billion, and the *real*-U.S. dollar exchange rate (sell side) in the commercial exchange market, as published by the Central Bank, stood at R$1.9832 to $1.00.

Following its decision to permit the *real* to float, Brazil began negotiations with the IMF on adjustments to the 1999-2001 economic program agreed in November 1998 and new economic targets in light of the new foreign exchange regime introduced in January 1999 and, on March 5, 1999, Brazil and the IMF announced that they had reached agreement. See "The Brazilian Economy—*Plano Real* and Current Economic Policy". On April 6, 1999, Brazil received a second disbursement, of approximately $4.9 billion, from the IMF, which was followed by an additional $4.9 billion in bilateral loans on April 9, 1999 under the IMF-led support package. After giving effect to the inflows from the IMF-led support package and an offering of debt securities by the Republic in April 1999 (see "Public Debt—Debt Crisis and Restructuring"), Brazil's international reserves stood at $44.3 billion on April 30, 1999, up from $35.5 billion at February 28, 1999 and $33.8 billion at March 31, 1999. At August 31, 1999, Brazil's international reserves stood at $41.9 billion.

Since 1994, debt management policy has aimed at lengthening the maturity of domestic public debt, as well as consolidating a domestic yield curve by means of selling fixed income government securities. The average maturity of debt was 149 days in December 1989, a period of high inflation, 430 days in September 1997, 463 days in July 1998 and 531 days in July 1999. In December 1989, 99% of the debt was indexed (floating-rate securities), compared to 42% in September 1997, 78% in July 1998 and 89% in July 1999. Non-residents holding of government securities is extremely low—approximately 1% of total outstanding domestic debt. The effort to consolidate the domestic yield curve through longer average maturities was temporarily interrupted by the Asian financial crisis in 1997 and the Russian financial crisis in 1998. Upon the return of normal market conditions, it is a major objective of the Government to proceed in the direction that was initiated with the launch of the *Plano Real* in July 1994.

The following table sets forth certain information regarding Brazil's international reserves at the dates indicated.

Table No. 23

International Reserves(1)

	As of December 31,				
	1994	1995	1996	1997	1998
	(in millions of dollars)				
Gold(2)	$ 1,418	$ 1,767	$ 1,381	$ 903	$ 1,353
Foreign Exchange	37,388	50,072	58,728	51,270	43,163
Total Gold and Foreign Exchange	38,806	51,839	60,109	52,172	44,516
Special Drawing Rights	0.4	1.0	1.0	0.5	40.2
Total Official Reserves	$38,806	$51,840	$60,110	$52,173	$44,556

(1) Foreign financial assets under control of and available to the monetary authorities.

(2) Dollar value calculated using a moving average of the London Gold PM Fixing prices quoted during the prior two months.

Source: Central Bank

Foreign Exchange Rates and Exchange Controls

The Brazilian foreign exchange system has been structured to enable the Government, through the Central Bank, to regulate and control foreign exchange transactions carried out in Brazil. Until February 1, 1999, there were two foreign exchange markets in Brazil: the commercial exchange market, on which most trade and financial transactions are carried out, and the floating exchange market (known as the "tourism dollar" market). The exchange rate in each market was established independently, resulting in different rates during some periods, and all transactions carried out in either of these markets were required to be conducted through banks (and other agents for the tourism market) authorized and monitored by the Central Bank.

The commercial exchange market consists primarily of (i) foreign currency transactions relating to export proceeds, which must be converted into *reais* through this market, since exporters are not allowed to maintain such proceeds outside Brazil; (ii) foreign currency transactions relating to import payments, which must be converted from *reais* through this market; and (iii) the conversion of *reais* and remittance of foreign currency from Brazil, which are permitted if the inflow is conducted through the commercial exchange market and registered at the Central Bank, a requirement applicable to capital investments in Brazil and to all types of foreign loans, as well as to any related dividend and interest remittances.

The floating exchange market was established in December 1988 with the objective of liberalizing certain transactions. Banks buy and sell currency in this market at freely negotiated rates. Transactions carried out through this market are mainly related to travel, unilateral transfers, certain services and gold operations. Since its creation, the premium of this market over the commercial exchange market has declined. After reaching values higher than 160.0% in 1989, the premium over the commercial exchange market rate at the end of July 1998 stood at 0.8%. The floating rate exchange market experienced significant growth with the addition of new types of transactions, including the development of an active interbank market. On August 31, 1994, the possibility of acquiring real estate abroad was extended to corporations (previously it was restricted to individuals). At the same time, the maximum value of investments abroad that the Brazilian banks could make without having previous authorization from the Central Bank was increased from $1 million to $5 million. In October 1994, certain limitations on the acquisition of foreign currency were eliminated, including those in connection with tourist and health care activities, education, scientific and cultural operations, asset transfers, software acquisitions and transactions involving credit cards. Due to the increased inflow of resources in this market, in August 1995 a tax of 7% was imposed on interbank operations with banking institutions abroad and on short-term investment into Brazil by non-residents which are not designated for any specific investment purposes. The tax rate was lowered to 2% at the end of April 1997 as a result of changes in the inflow of foreign resources and to 0.5% on April 18, 1998. In May 1996, the Government made significant changes affecting floating exchange market transactions. Among other changes, the maximum amount of foreign exchange that could be remitted abroad was increased, the requirement that Brazilian tourists purchase foreign exchange within one year prior to traveling abroad was eliminated and the use of credit cards in Brazil and abroad for obtaining foreign exchange was authorized.

Until January 15, 1999, whenever the supply and demand for foreign currency establish exchange rates incompatible with the Government's economic policy goals, the Central Bank could intervene in the market to adjust liquidity conditions by means of auctions for the purchase, sale or simultaneous purchase and sale (so-called spread auctions) of foreign currency. Those auctions were conducted through dealer institutions, although the Central Bank could deal directly with any of the institutions authorized to deal in the foreign exchange market. Under the terms of a spread auction, participating institutions were obliged to set purchase and sale rates. The use of spread auctions beginning in June 1995 constituted an important mechanism for maintaining exchange rates closer to market conditions, thereby helping to avoid speculative movements against the Brazilian currency. In addition, the number of institutions eligible to participate in the auctions was increased from 20 to 60, in an attempt to make the auctions more representative.

Under Resolution No. 2,110 of the National Monetary Council, the Central Bank had an obligation to sell U.S. dollars in the foreign exchange market whenever the *real* reached parity with the U.S. dollar. In response to deterioration in Brazil's current account, on March 6, 1995 the Central Bank formalized an exchange band system for both the commercial foreign exchange market and floating foreign exchange market, pursuant to which the *real* was permitted to float against the U.S. dollar within bands established by the Central Bank. Under the exchange band system, the Central Bank was committed to intervene in the market whenever rates approached the upper and lower limits of the band. Such commitment did not eliminate the possibility of the Central Bank intervening when necessary to avoid extreme oscillations in the exchange rate.

The Central Bank periodically adjusted the exchange band to permit the gradual devaluation of the *real* against the U.S. dollar. The initial band announced on March 6, 1995 was R$0.86 to R$0.90 per U.S. dollar. On March 10, 1995, a new band was announced: R$0.88 to R$0.93 per U.S. dollar. On June 22, 1995, the Central Bank announced that the *real* would be permitted to trade between R$0.91 and R$0.99 per U.S. dollar. On January 30, 1996, the range within which the *real* would be permitted to trade in relation to the U.S. dollar was changed to between R$0.97 and R$1.06 per U.S. dollar. The fourth exchange band, announced on February 18, 1997, had an upper limit of R$1.14 per U.S. dollar and a lower limit of R$1.05 per U.S. dollar. The fifth exchange band, announced on January 20, 1998, had an upper limit of R$1.22 per U.S. dollar and a lower limit of R$1.12 per U.S. dollar.

On January 13, 1999, Gustavo H.B. Franco, the president of the Central Bank and one of the architects of the *Plano Real*, resigned and was replaced by Francisco Lopes, who attempted a controlled devaluation of the *real* by widening the band within which the *real* was permitted to trade. Subsequent Central Bank intervention failed to keep the *real*-U.S. dollar exchange rate within the new band, however, and on January 15, 1999, the Central Bank announced that the *real* would be permitted to float, with Central Bank intervention to be made only in times of extreme volatility. Following that announcement, the value of the *real* against the U.S. dollar declined approximately 21% from its level on January 12, 1999. See "The Brazilian Economy—*Plano Real* and Current Economic Policy".

To minimize excessive exchange rate volatility and reduce the inflationary effects of the devaluation of the *real*, the Central Bank raised its assistance rate (TBAN) to 41% from 36% on January 19, 1999, and the Central Bank intervened in the market to adjust the Federal Funds Rate (*taxa Over/Selic*) to 32% on

January 19, 1999 from 29.8% the previous day. The *Over/Selic* rate was further increased to 35.5% on January 28, 1999 and 37.0% on January 29, 1999. The value of the *real* continued to decline, however; as of January 31, 1999, the *real*-U.S. dollar exchange rate (sell side) in the commercial exchange market, as published by the Central Bank, stood at R$1.9832 to $1.00.

On February 2, 1999, when the cumulative devaluation (since January 13, 1999) of the *real* against the U.S. dollar exceeded 40%, the Government designated Armínio Fraga Neto to replace Francisco Lopes as president of the Central Bank. Following Mr. Fraga's confirmation on March 3, 1999, the Central Bank eliminated the TBC and TBAN rates, giving primacy to the *Over/Selic* rate; because the Central Bank can influence the *Over/Selic* rate on a daily basis through its participation in auctions, repurchase transactions and reverse repurchase transactions, the *Over/Selic* rate permits the Central Bank to react more quickly to changes in market conditions. The Central Bank also increased the *Over/Selic* rate to 45% from 39%. The Central Bank subsequently reduced the *Over/Selic* rate to 42% on March 25, 1999, 39.5% on April 6, 1999, 34% on April 15, 1999, 32% on April 29, 1999, 29.5% on May 10, 1999, 27% on May 13, 1999, 23.5% on May 20, 1999, 22% on June 9, 1999 and 21% on June 24, 1999, citing lower-than-expected inflation and improved expectations for the economy. The *Over/Selic* rate was further reduced to 19.5% on July 28, 1999 and 19% on September 22, 1999.

The adoption of the foreign exchange rate regime described above produced the unification, as of February 1, 1999, of the previously separate commercial and floating rate foreign exchange markets. The *real*-U.S. dollar exchange rate (sell side) in the commercial exchange market on August 31, 1999, as published by the Central Bank, stood at R$1.9159 to $1.00, down from R$1.7892 to $1.00 on July 31, 1999 and R$1.7695 to $1.00 on June 30, 1999.

The following table sets forth average exchange rates recorded in the commercial exchange market (sell side) on the last day of the periods indicated.

Table No. 24

Commercial Exchange Rates (sell side)

	Spot Rate(1)	Foreign Currency Basket(2)
	(*reais* per dollar)	
1994—December	0.8460	74.6
1995—December	0.9275	84.2
1996—December	1.0394	82.9
1997—December	1.1164	78.2
1998—December	1.2087	82.8
1999—January	1.9832	101.3
February	2.0648	118.2
March	1.7220	111.3
April	1.6607	99.5
May	1.7240	n.a.
June	1.7695	n.a.
July	1.7892	n.a.
August	1.9159	n.a.

(1) The average rate on the last day of month in the commercial exchange market.

(2) An index of the real exchange rate of a basket of fifteen currencies weighted by the share of the total Brazilian exports to all fifteen countries involved represented by Brazilian exports to each such country. The national currency used was the average exchange selling rate and the deflator was IPA-DI (Wholesale Prices). For other countries the deflator was also a wholesale price index or a comparable indicator (June 1994 = 100).

Source: Central Bank

Brazilian law provides that, whenever there is a serious imbalance in Brazil's balance of payments or serious reasons to foresee such an imbalance, the Government may, for a limited period of time, impose restrictions on the remittance to foreign investors of the proceeds of their investments in Brazil, as it did for approximately six months in 1989 and early 1990, and on the conversion of Brazilian currency into foreign currencies. See "Public Debt—Debt Crisis and Restructuring".

THE FINANCIAL SYSTEM

General

On July 1, 1994, the *real* (plural "*reais*") replaced the *cruzeiro real* as the lawful currency of Brazil, with each *real* exchangeable for 2,750.00 *cruzeiros reais*. The *cruzeiro real* had replaced the *cruzeiro* as the lawful currency of Brazil on August 1, 1993, with each *cruzeiro real* exchangeable for 1,000 *cruzeiros*. The *cruzeiro* had replaced the *cruzado novo* as the lawful currency of Brazil under the Collor Plan of March 15, 1990, with each *cruzeiro* exchangeable for one *cruzado novo*. The *cruzado novo* had replaced the *cruzado* as the lawful currency of Brazil under the Summer Plan of January 16, 1989, with each *cruzado novo* exchangeable for 1,000 *cruzados*. The *cruzado* had replaced the *cruzeiro* as the lawful currency of Brazil under the Cruzado Plan of February 28, 1986, with each *cruzado* exchangeable for 1,000 *cruzeiros*.

The Brazilian financial system is composed of several types of public and private sector financial institutions. On February 28, 1999, it included 177 multiple service banks, 29 commercial banks, 21 investment banks, and numerous savings and loan, brokerage, leasing and financial institutions. The high inflation environment in Brazil stimulated Brazilian financial institutions to develop sophisticated systems and mechanisms for settlement and collection of transactions and for general cash and treasury management.

Public sector banking institutions play an important role in the banking industry, the largest segment of the financial system. Public sector banks accounted for 56.3% of the banking system's total demand deposits and 43.8% of total assets at February 28, 1999. A significant portion of the activities of federal and State banks involves the lending of government funds to industry and agriculture. See "—Public Financial Institutions".

Between 1989 and 1994, as demand for credit declined and inflation increased, the financial sector profited from financial gains derived from investing funds in high-yielding, inflation-adjusted government instruments and from short-term financial intermediation. Earnings and return on equity were fairly constant for private sector banks. The performance of the public sector banks, however, was less consistent, reflecting the fact that, in addition to their normal commercial activities, such banks also extended credit in accordance with government economic policy objectives. At December 31, 1998, the average leverage level for the Brazilian banking system as a whole was relatively low at 2.8 times shareholders' equity, and Brazilian private sector financial institutions were generally well capitalized.

Under the *Plano Real*, a lower inflation environment has led to increased investment and demand for credit. At first, the *Plano Real* had some negative impact on the earnings of the banking sector by eliminating gains previously enjoyed under conditions of high inflation, particularly for those financial institutions under Government control that have high operating cost structures and State-owned banks that have a large portfolio of State government-issued securities. Some State-owned banks that were dependent on readily available overnight interbank funds have faced difficulties, and, in late December 1994, the Central Bank assumed administrative control over BANESPA and BANERJ. Some State governments and the Central Bank have been discussing the possibility and means of privatizing their respective financial institutions. Significant dispositions, as of December 31, 1998, included: (i) BANERJ, which was sold to Banco Itaú S.A. on June 26, 1997 for R$331.0 million; (ii) Banco de Crédito Real de Minas Gerais S.A.—Credireal, which was sold to Banco de Crédito Nacional S.A.—BCN on August 7, 1997 for R$121.1 million; (iii) Banco do Estado de Minas Gerais S.A.—BEMGE, which was sold to Banco Itaú S.A. on September 14, 1998 for R$583.0 million; and (iv) Banco do Estado de Pernambuco S.A.—BANDEPE, which was sold to Banco ABN AMRO on November 17, 1998 for R$182.9 million. In addition, the Republic is in the process of liquidating certain other State financial institutions such as Produban, the State bank of Alagoas, and the State banks of Amapá, Mato Grosso and Rio Grande do Norte. The State Bank of Rondônia placed itself in liquidation on August 14, 1998.

On November 27, 1996, the federal Government and the State of São Paulo signed an agreement that provides for, among other things, the restructuring of the State's R$16.8 billion debt to BANESPA as part of a larger restructuring of the State's debt pursuant to Law No. 9,496 of September 11, 1997. Under the agreement, 20% of the State's debt restructured thereunder is to be repaid through the transfer by the State to the federal Government of certain assets to be privatized. The remaining 80% of such State debt is to be paid in monthly installments over a 30-year period. This agreement made possible the federal takeover of BANESPA on December 23, 1997. See "The Brazilian Economy—Changes in the Relationship between the Federal and Local Governments".

The Central Bank has sold special Central Bank bills (LBC-E) on a forward basis to some State-owned banks, receiving State government-issued securities as collateral until the cost of funds to those institutions is normalized. Such transactions, which are done for renewable 30-day periods, reached an outstanding balance of $31.6 billion on January 1, 1997. The outstanding balance of such transactions on December 31, 1998 was $7.6 billion. In addition, to counteract and contain any localized liquidity problems of Brazilian financial institutions in the course of their adaptation to the new financial conditions under the *Plano Real*, the Central Bank made short-term "liquidity loans" available to targeted Brazilian financial institutions. In February 1999, the average daily amount outstanding in the form of liquidity loans was R$421 million.

In July 1996, the Government also increased by R$8 billion the capital of Banco do Brasil, a Government-controlled bank and Brazil's largest commercial bank, which reported a 1995 loss in excess of R$4 billion and a 1996 loss of R$7.5 billion. This capital increase was funded through the issuance of National Treasury Notes (R$6.5 billion) and by investments made in Banco do Brasil by PREVI (R$1 billion) and BNDESpar (R$500 million). See "—Public Financial Institutions—Banco do Brasil".

The critical importance of financial management skills under conditions of high inflation, and the availability of profits from financial intermediation activities, led to the proliferation of financial institutions during the 1980s and early 1990s. The subsequent reduction of Brazil's inflation rate brought about by the *Plano Real* has curtailed the profits Brazilian banks had previously earned from investing deposits at inflated interest rates and has made it more difficult for certain financial institutions to survive. From the implementation of the *Plano Real* to December 31, 1998, 127 financial institutions, of which eight had assets over $300 million, were the subject of Central Bank intervention; 108 of these troubled institutions had ceased operations. In order to assist distressed banks and strengthen the financial system, the Government instituted on November 3, 1995 the Program of Incentives for Restructuring and Strengthening of the National Financial System (PROER). See "—Monetary Policy and Money Supply". Among other measures, PROER creates special lines of credit for financial institutions and provides incentives for institutions to merge and reorganize by permitting the amortization of goodwill and the write-off of non-performing loans. Under PROER, institutions receiving support are required to pledge collateral to the Central Bank having a value of at least 120% of the amount of the disbursement received. The collateral pledged by institutions participating in PROER generally has consisted of Government debt instruments such as Par Bonds and obligations of the *Fundo de Compensação de Variações Salariais* (FCVS). See "Public Debt—Housing Compensation Fund for Salary Fluctuation (*Fundo de Compensação de Variações Salariais*)". Debt instruments so pledged are valued at their full face amount. Equity securities may also be pledged; such securities are valued based on several criteria, including liquidity. Interest accrues on the disbursements at a rate of 2% over the rate of interest on the underlying collateral and is payable at the same time interest is payable on the underlying collateral. Under the PROER program, the Central Bank may reschedule or otherwise restructure the credits granted. If a default should occur by any of the institutions receiving support under PROER, the Central Bank will have the option to hold the collateral to maturity or to sell the pledged collateral in the secondary market, which may result in the sale of such instruments at a discount.

To date, PROER funds have been used to finance the acquisition of certain assets of seven private banks, including Banco Nacional S.A., Banco Antônio de Queiroz S.A., Banco Econômico S.A., Banorte S.A., Banco Mercantil S.A., Banco Pontual S.A. and Banco Bamerindus S.A. ("Banco Bamerindus"), by seven other private banks and one federal institution, CEF. In August 1995, the Central Bank intervened in the operations of Banco Econômico S.A. ("Banco Econômico"), a large private sector bank operating primarily in the State of Bahia, and, in early May 1996, approved the transfer of that bank's principal operating assets and liabilities of Banco Econômico to Excel Banco S.A. Banco Econômico was subsequently placed under nonjudicial liquidation. In November 1995, the Central Bank assumed control of Banco Nacional S.A. ("Banco Nacional"), then Brazil's sixth largest private sector bank, and effected the sale to Unibanco—União de Bancos Brasileiros S.A. of a substantial portion of the assets, liabilities and operations of Banco Nacional. The Central Bank also strengthened its supervision of the banking system, in part as a result of allegations that Banco Nacional had fraudulently misstated the value of its capital and revenue by a significant amount. Like Banco Econômico, Banco Nacional was subsequently placed under nonjudicial liquidation. In March 1997, as a result of continuing liquidity and related problems, the Central Bank intervened in Banco Bamerindus, then Brazil's fourth largest private sector bank, and transferred selected assets and liabilities to a newly created, wholly owned Brazilian subsidiary of the Hongkong and Shanghai Banking Corporation, which had previously been a minority shareholder of Banco Bamerindus. The restructuring of Banco Bamerindus was financed, in part, through disbursements under PROER in an aggregate amount of approximately R$4.3 billion, including R$2.5 billion to finance the acquisition of Banco Bamerindus' real estate holdings by CEF.

From the introduction of PROER in November 1995 to December 31, 1998, the Central Bank has made gross disbursements of approximately R$21.0 billion available, primarily for the restructuring of Banco Nacional, Banco Econômico and Banco Bamerindus; this amount does not reflect any assistance that may eventually be provided to other banks which may become eligible for assistance in the future. Through December 31, 1998, the institutions receiving support under PROER have made reimbursements of PROER reserves in the aggregate of approximately R$18.3 billion to the Central Bank. The Government estimates that the aggregate cost of the PROER program as conducted to date will not exceed approximately 1% of GDP. The eight institutions that received PROER disbursements, including Banco Econômico, Banco Mercantil and Banco Nacional, have been sold to private financial institutions. As a result of such liquidations, the Central Bank has succeeded to the rights in the assets pledged to secure the PROER disbursements made to these institutions and may exercise its rights in such collateral in the manner described above.

On February 28, 1997, the National Monetary Council adopted Resolution No. 2,365, establishing the Support Program for the Reduction of State Public Sector in Banking Activity *("Programa de Incentivo à Redução do Setor Público Estadual na Atividade Bancária" or "PROES").* PROES provides for three special lines of financial assistance. The first line releases resources backed by collateral consisting of securities or rights related to operations under the administration of the National Treasury or of agencies of the federal Government. The second line allows State financial institutions to restructure their portfolio of assets and/or their respective liabilities. The third line involves the assumption by federal financial institutions of State financial institutions' liabilities to the public. The first two lines were implemented by Central Bank Circulars Nos. 2,743 and 2,744, both dated February 28, 1997, and the third line was implemented by Central Bank Circular No. 2,745 dated March 18, 1997, as amended by Circular 2,871 dated March 4, 1999.

As of December 31, 1998, 40 State financial institutions had sought PROES assistance, with a majority electing to be privatized or converted into a development agency; only six financial institutions chose to obtain PROES assistance under the second line. In December 1998, an institution controlled by the State of Rio Grande do Sul commenced operations as the first such converted development agency.

In addition to establishing PROER and PROES, the Government instituted a deposit insurance system on November 16, 1995 and issued a provisional measure in August 1996 establishing a program to restructure Brazil's State banks. See "The Brazilian Economy—Changes in the Relationship between the Federal and Local Governments" and "—Regulation by Central Bank". The President of the Republic also issued Provisional Measure No. 1,394 of February 9, 1996, subsequently adopted as Law No. 9,447 of March 14, 1997, concerning the liabilities of the controlling shareholders, accounting firms and independent auditors in connection with the intervention, extrajudicial liquidation or establishment of a provisional administrative regime for financial institutions. Controlling shareholders may be held jointly liable for wrongful acts involving the financial institutions they control, independent of claims based on negligence or fraud. Independent auditors can also be held liable for their fraudulent actions or omissions while rendering services to financial institutions, and the assets of such auditors may be subject to attachment if liability is found.

Institutional Framework

The basic framework for the Brazilian financial system was established in 1964 pursuant to Law No. 4,595 (the "Banking Reform Law"), which created the National Monetary Council (the "CMN"), the senior body responsible for currency and credit policies.

The legal measures that introduced the *real* as the new legal currency also modified the composition of the CMN, reducing it to three members: the Minister of Finance, the Head of the Secretariat of Planning, Budget and Coördination and the President of the Central Bank.

The Central Bank is an autonomous government entity, administered by a board of directors, all of whom are appointed by the President of the Republic, subject to confirmation by the Senate. The main role of the Central Bank is to implement the currency and credit policies established by the CMN.

The Brazilian Securities Commission *(Comissão de Valores Mobiliários* or "CVM") is responsible for regulating the country's stock exchanges, protecting investors and shareholders against fraud or manipulation with respect to securities traded on such exchanges and promulgating accounting and reporting rules to ensure the availability to the public of information on securities and their issuers.

Monetary Policy and Money Supply

The CMN's current policy is to maintain a tight credit policy in an attempt to control liquidity and maintain a low rate of inflation. The current monetary policy reflects, in part, a substantial increase in the demand for base money due in large part to the significant remonetization following the issuance of the *real*. Accordingly, the CMN establishes a target for the average monetary base for each quarter. For the fourth quarter of 1998, the target was set at a range between R$34.6 billion and R$40.7 billion.

In April 1995, the CMN implemented a number of measures to restrain domestic demand, including: (i) an increase in the reserve requirement for banks; (ii) an increase in the IOF on bank loans (including overdrafts, credit card debts and promissory notes) to natural persons to 18.0% annually from 6.0%; (iii) a limitation on the purchase and trading of commercial paper by banks; and (iv) a prohibition on accepting checks as security for short-term bank loans. The IOF on bank loans has since been reduced to 0%. See "Balance of Payments and Foreign Trade—Foreign Investment". Since July 1994, in its effort to support the *Plano Real* and contain inflation, the Central Bank has taken a number of steps to control credit and monetary aggregates. The maturity of consumer credit extended by financial institutions has been restricted to 90 days, reserve requirements have been imposed on several types of transactions, and other credit restrictive measures have been adopted. See "—Reserve Requirements".

The Government has also attempted to control liquidity and regulate the monetary impact of increases and reductions in its international reserves through issuances and repurchases of its domestic debt securities. As its international reserves declined during the first half of 1995, the Government provided liquidity by repurchasing its domestic debt securities, thereby increasing the supply of base money. As its international reserves increased during the second half of 1995, the Government sought to sterilize the monetary impact of that increase by issuing new domestic debt securities, thereby reducing the supply of base money and reversing the process of remonetization that occurred following the issuance of the *real*. The interest rates for such domestic debt securities (a real rate of 26.6% per annum as of December 31, 1998) significantly exceeds the Republic's rate of return on the investment of its international reserves.

In order to reduce consumption of durable goods, in May 1997, the Government issued Decree No. 2,219, increasing the annual IOF from 6% to 15% annually on extensions of credit (including overdrafts, credit card debt and promissory note) to individuals. In July 1998, the Government reduced the annual IOF to 6% from 15%.

Open-Market Transactions. The Central Bank's open-market transactions began over twenty years ago and became the most important instrument of monetary policy as the domestic government securities market experienced significant development in trading volume, operating capacity and sophistication. At the end of each day, the Central Bank, through open-market transactions, consisting primarily of the use of repurchase agreements, seeks to ensure that its interest rate objective is achieved and that financial institutions are provided with sufficient liquidity. The main instruments used in open-market transactions are federal Government and Central Bank bonds.

Indexation and Interest Rates. Prior to January 31, 1991, Brazil used a system of monetary correction, or indexation, designed to correct some of the distortions caused by inflation. Such indexation involved periodic adjustments in accordance with the movements of price indices for financial assets. Rents, past due taxes, fees and other social contributions, corporate assets, liabilities and net worth accounts, among others, were also readjusted by indexation. See "The Brazilian Economy—Prices".

On June 20, 1996, the Central Bank created the Central Bank Basic Rate (TBC), which was calculated monthly and established by the Central Bank's Monetary Policy Committee. In its role as the successor to the Brazilian prime rate, TBC served as a guidepost for daily intervention by the monetary authorities in the open market. In August 1996, the Monetary Policy Committee instituted a second rate, the Central Bank Assistance Rate (TBAN). Both the TBAN and the TBC applied to discount window operations and perform a signaling function for the markets as to the Central Bank's policy intentions.

The "Over/Selic" rate—a market-determined overnight rate for operations with federal bonds which determines the interest rate on debt issued by the Central Bank and the Government in a manner similar to the U.S. federal funds rate—floated in the range between the TBAN (upper limit) and the TBC (lower limit) in a scheme similar to that used by the German Bundesbank.

On March 3, 1999, the Central Bank eliminated the TBC and TBAN rates and increased the *Over/Selic* rate to 45% from 39%. The Central Bank subsequently reduced the *Over/Selic* rate to 42% on March 25, 1999, 39.5% on April 6, 1999, 34% on April 15, 1999, 32% on April 29, 1999, 29.5% on May 10, 1999, 27% on May 13, 1999, 23.5% on May 20, 1999, 22% on June 9, 1999 and 21% on June 24, 1999, citing lower-than-expected inflation and improved expectations for the economy. The *Over/Selic* rate was further reduced to 19.5% on July 28, 1999 and 19% on September 22, 1999. Following the decision to permit the *real* to float freely, the Government announced that it intends to pursue a monetary policy based on inflation targeting. In June 1999, the Government announced inflation targets of 8% in 1999, 6% in 2000 and 4% in 2001, as measured by the IBGE's IPCA index. See "The Brazilian Economy—*Plano Real* and Current Economic Policy".

Time Deposits. Since September 1996, there has been a gradual reduction in the percentage of reserves required to be invested in government securities, and the cash component of the reserve requirement has been increased in the same proportion. In February 1997, the requirement to hold government securities was eliminated, and the cash reserve requirement was set at 20%.

Formerly, the Brazilian monetary authorities relied on short-term National Treasury Bonds *(Bônus do Tesouro Nacional)* as the principal instrument for indexation. As that instrument was phased out, the *Taxa Referencial* ("TR") was created for purposes of indicating the prevailing interest rate. The TR is calculated by the authorities periodically, based on the average daily rate for bank certificates of deposit. Based on current rates rather than historical rates, the TR was intended to reduce the influence of past inflation and more accurately reflect future inflation than predecessor indices. In January 1994, the Government revised the methodology for the calculation of the TR in order to increase the incentive to deposit money in savings accounts. The TR is currently derived from the Basic Financial Rate (*Taxa Básica Financeira* or "TBF"), which is calculated by the Central Bank from the weighted average of the rates offered by financial institutions on their certificates of deposit. The TBF so calculated is adjusted by a reduction factor in determining the TR. The reduction factor may occasionally be modified as a consequence of the changes in the real interest rate and the tax rate on the gross earnings of the certificates of deposit.

Reserve Requirements. All depositary institutions, commercial banks, multiple service banks, investment banks, development banks, savings and loans and financial institutions are required to satisfy reserve requirements set by the Central Bank. These reserve requirements are applied to a wide range of banking activities and transactions, such as demand deposits, savings deposits, time deposits, debt assumption transactions, automatic reinvestment deposits, funding transactions, repurchase agreements and export notes. Generally, banks are required to deposit in a non-interest-bearing account at the Central Bank: (i) 65% of the average daily balance of demand deposits in excess of R$2 million; and (ii) 60% of the average daily balance of bank drafts, collections of receivables, collections of tax receipts and proceeds from the realization of guarantees granted to financial institutions in excess of R$2 million. In addition, banks are required to deposit in an interest-bearing account at the Central Bank, on a weekly basis, an amount in cash equal to 15% of the average daily balance of savings accounts, calculated on a weekly basis. Finally, financial institutions are required to deposit with the Central Bank federal bonds having an aggregate principal amount at least equal to 10% of the average daily balance of time deposits in excess of R$30 million.

Beginning on January 1, 1995, the Brazilian banking system became subject to the risk-based capital adequacy system of the Basle Accord adopted under the auspices of the Bank for International Settlements. See "—Regulation by Central Bank—Capital Adequacy, Liquidity and Concentration Limits".

The following table sets forth selected information regarding percentage changes in the monetary base and money supply for the periods indicated.

Table No. 25

Percentage Increases in Monetary Base and Money Supply

	Year Ended December 31,				
	1994	1995	1996	1997	1998
Monetary Base(1)	3,322.4%	22.6%	(8.7)%	60.8%	23.1%
M1(2)	2,586.2	25.1	4.6	58.9	7.1
M2(3)	965.3	47.7	55.6	21.4	24.5

(1) Monetary base represents Central Bank liabilities, including currency and deposits held by commercial banks.
(2) M1 is currency plus demand deposits.
(3) M2 is M1 plus Financial Investment Funds (*Fundos de Aplicação Financeira* or FAF), short-term fixed-income funds (FRF-CP), short-term, financial investment funds (FIF-CP), federal, state and municipal securities and special earnings deposits less FAF demand deposits and federal, state and municipal securities in the portfolios of the Central Bank, FAF, FRF-CP, FIF-CP and other financial institutions.

Source: Central Bank

In an attempt to maintain consumption at levels consistent with the price stabilization process, the Government gave special attention to interest rate policy. The level of reserve requirements imposed on demand deposits, time deposits, savings deposits and on credit operations was the main factor responsible for the maintenance of high interest rates in Brazil in 1995.

Other measures were adopted to promote monetary restraint and credit control. In June 1995, in an effort to lengthen the term of financial market operations, the Government instituted the financial operations base rate (TBF). The TBF applies to financial operations with terms equal to or greater than 60 days. Financial institutions were authorized to accept time deposits with an automatic reinvestment feature and interest payable quarterly based on the TBF.

In addition, with the implementation in January 1997 of the CPMF, the 0.20% levy on certain financial market transactions, the Government expects a significant shift of funds from short-term investments to longer term investment options. In March 1999, the National Congress approved an increase in the CPMF rate to 0.38% for 1999. See "The Brazilian Economy—*Plano Real* and Current Economic Policy".

In July 1995, the CMN adopted new measures governing certain investment funds. The Central Bank authorized the formation of new mutual funds, called financial investment funds (FIFs). The FIFs were created with the aim of lengthening the term of financial investments. To accomplish this goal, reserve requirements are levied on the net worth of the FIF. Short-term FIFs (up to 29 days) have a reserve requirement of 40%; 30- to 59-day FIFs, 5%; and 60-day-plus FIFs, 0%. Between August and December 1996, the reserve requirement on a short-term FIF's net worth was gradually increased from 42% to 50% in accordance with Circular No. 2,703, dated July 3, 1996.

Monetary and credit policy was eased somewhat in the second half of 1995 in order to increase liquidity. These measures included reducing the required level of reserves and increasing the term of credit operations from three months to six months. In April 1996, the term requirement was abolished.

In order to strengthen the financial system and assist distressed financial institutions, the Government adopted PROER on November 3, 1995. The PROER program seeks to ensure the liquidity and solvency of the financial system while safeguarding the interests of depositors and investors. It creates special lines of credit and defines measures aimed at encouraging administrative, capital and operational reorganization of financial institutions through merger, consolidation and asset shrinkage. Among the incentives included in the program are tax rules governing the treatment of capital gains and recognition of losses on problem credits. Participating institutions may obtain Central Bank financing at below-market rates. In addition, to help support the financial system, the Government instituted a deposit insurance system in Brazil through the creation of the Credit Guaranty Fund ("FGC") in November 1995. See "—General" and "—Regulation by Central Bank".

Limitation of Public Sector Debt

Since May 1990, the CMN has taken various measures to limit expansion of credit in the public sector. In July 1993, the CMN mandated the creation by the Central Bank of a Public Sector Operations Registration System designed to improve credit controls. The CMN has also limited the ability of public sector financial entities to issue additional public indebtedness.

In 1993, the Constitution was amended to limit the amount of securities debt that the States, the Federal District and municipalities could incur. Constitutional Amendment No. 3 dated March 17, 1993 limits, until December 31, 1999, the issuance of securities by the States, the Federal District and municipalities to the amount necessary to roll over their maturing securities.

Pursuant to Article 33 in the Constitution Act of Transitory Dispositions, the Senate was permitted to authorize until July 1, 1997 certain additional issuances of securities by States, the Federal District and municipalities for the limited purpose of paying final judgments. In February 1997, a Parliamentary Committee of Inquiry (the "CPI") began an investigation of allegations that certain States and municipalities may have misused the proceeds of certain debt securities which were issued by such States and municipalities to pay final judgments pursuant to Article 33. On August 19, 1997, the CPI issued a report setting forth recommendations for corrective action. As a consequence of the CPI, the Senate adopted Resolution No. 78 of 1998 on July 1, 1998, which severely restricts the issuance of debt securities by States and municipalities. The total amount of securities of the States and municipalities outstanding as of September 30, 1997 was approximately R$57.0 billion, of which an estimated R$11.9 billion was issued to pay final judgments under Article 33.

On June 29, 1998, the National Monetary Council of Brazil issued Resolution No. 2,515 ("Resolution No. 2,515"), which establishes certain conditions that must be observed with respect to the external credit operations of States, the Federal District, municipalities, and their respective agencies, foundations and companies. Resolution No. 2,515 requires, among other things, that (i) the proceeds of such external credit operations be used to refinance outstanding domestic financial obligations of the issuer, with preference given to those domestic obligations having a higher cost or shorter term than the external debt and, pending such application, remain on deposit in an escrow account in a form specified by the Central Bank and (ii) the total amount of the contractual obligation be subject to monthly deposits in an escrow account in a form specified by the Central Bank, with each monthly deposit to be equal to the total debt service obligation (including principal and interest), divided by the number of months that the obligation is to be outstanding (iii) the foreign creditor (underwriter, in case of a securities issue) be a financial institution that traditionally maintains a relationship with Brazil or that has a risk rating equal to or higher than "BBB", according to the international rating agencies; and (iv) the contracts relating to such operations contain a clause expressly providing that the borrower's obligations are not guaranteed by the federal Government and that the creditors acknowledge that they will not be entitled to receive any funds from the federal Government for such operations.

Public Financial Institutions

Brazil's principal public sector financial institutions are Banco do Brasil, BNDES and CEF, all federal institutions, together with a number of state institutions.

Banco do Brasil. Banco do Brasil, the main lender to the rural sector, is Brazil's largest commercial bank. It is organized as a mixed-capital company, with the federal Government holding a majority of its voting shares, and is subject to legislation applicable to private sector entities, including all labor and tax legislation. Banco do Brasil functions as a private commercial bank, although it does engage in some lending programs which implement certain policies established by the CMN. In March 1996, Banco do Brasil announced a significant restructuring of the bank following a 1995 loss in excess of R$4 billion and a 1996 first half loss of R$7.8 billion. On March 20, 1996, the Government enacted Provisional Measure No. 1,367, authorizing the National Treasury to increase the capital of Banco do Brasil by up to R$8 billion. Such amount was funded by issuance of National Treasury Notes (R$6.5 billion) and by investments made in Banco do Brasil by PREVI (R$1 billion) and BNDESpar (R$500 million). In October 1997, the Government announced that it is studying the possibility of selling up to 23% of the voting shares and up to 69.8% of the nonvoting preferred shares of Banco do Brasil. The Government would continue to retain a controlling interest in the bank following the sale. On January 31, 1999, Banco do Brasil had assets of approximately R$124.7 billion and a net worth of approximately R$6.6 billion.

BNDES. BNDES, the federal Government-controlled development bank, is primarily engaged in the provision of medium- and long-term financing to the Brazilian private sector, particularly to industry, either directly or indirectly through other public and private sector financial institutions. BNDES is also responsible for administering the federal Government's privatization program. On January 31, 1999, BNDES had assets of approximately R$81.2 billion and a net worth of approximately R$10.3 billion.

CEF. CEF, a savings bank controlled by the federal Government, is Brazil's largest multiple service bank and the principal agent of the Housing Finance System. CEF is involved principally in deposit-taking and the provision of financing for housing and related infrastructure. Its assets on January 31, 1999 were approximately R$116.4 billion, and its net worth stood at approximately R$3.6 billion.

Others. Other federal financial institutions are Banco da Amazônia and Banco do Nordeste do Brasil; Banco Meridional was purchased on December 4, 1997 by Bozano Simonsen for R$265.7. In addition, a number of commercial and multiple service banks are controlled by the several States. Several State banks, including BANESPA and BANERJ, were put under the administrative control of the Central Bank in December 1994. Banco Itaú S.A. has purchased two State Banks—BANERJ on June 26, 1997 for R$331.0 million and Banco do Estado de Minas Gerais (BEMGE) on September 14, 1998 for R$583.0 million—and control of BANESPA passed to the federal Government on December 31, 1997 in connection with the restructuring of the State of São Paulo's R$16.8 billion debt to BANESPA. In addition, Banco do Estado de Pernambuco S.A.—BANDEPE was sold to Banco ABN AMRO on November 17, 1998 for R$182.9 million. See "—General" and "The Brazilian Economy—Changes in the Relationship between the Federal and Local Governments".

Most of the States own or indirectly control the majority of the shares of a bank. State-owned or -controlled banks were sometimes used by State governments to finance the economic and political activities of State governments; such practices resulted in the making of loans that might not otherwise have been made on strictly commercial criteria. Some Brazilian State-owned or -controlled banks have at times required the direct or indirect financial assistance of the Central Bank. See "—General". With the introduction of a number of reforms by the Central Bank in 1993, in particular regulations involving State-owned or -controlled bank lending practices, those institutions were restricted from granting credits to their controlling entities.

In August 1996, the federal Government issued Provisional Measure No. 1,514 dated August 7, 1996 (subsequently superseded by Provisional Measure Nos. 1,556-6, 1,590-15, 1,654-24, 1,702-27, 1,702-30, 1,773-32 and 1,900-91) which established a program to facilitate the restructuring of Brazil's State banks. This provisional measure, among other things, permitted the Republic, in its sole discretion, to (i) acquire control of a financial institution, exclusively for its privatization or dissolution, (ii) finance the closure of the financial institution or its transformation into a non-financial institution or development agency or (iii) finance the prior arrangements necessary for the privatization of the financial institution or to guarantee any credit by the Central Bank for the same end, in accordance with rules to be promulgated by the National Monetary Council. See "The Brazilian Economy—Changes in the Relationship between the Federal and Local Governments".

In conjunction with efforts of the federal Government to assist the States under the Support Program for the Restructuring and Fiscal Adjustment of States and the assistance provided by the federal Government to the States in refinancing certain State debt, several State banks have come under the supervision of the Central Bank under nonjudicial liquidation by the Central Bank (like Banco do Estado do Rio de Janeiro S.A. and Banco do Estado de Alagoas S.A.), *"Regime de Administração Especial Temporária"*—RAET (like Banco do Estado do Amapá S.A. and Banco do Estado de Mato Grosso S.A.) and judicial liquidation (like Banco do Estado de Rondônia S.A.).

Private Sector Financial Institutions

Effective September 21, 1988, Brazil permitted the establishment of multiple service banks. Multiple service banks are licensed to provide a full range of commercial banking, investment banking (including securities underwriting and trading), consumer financing and other services, including fund management and real estate finance. As of February 28, 1999, there were 157 private multiple service banks operating in Brazil.

Private sector financial institutions include commercial banks, investment banks, multiple service banks and other financial institutions. Brazil's 26 private sector commercial banks are engaged in wholesale and retail banking. They are particularly active in taking demand deposits and lending for short-term working capital purposes. Brazil's 21 investment banks are engaged primarily in collecting time deposits, specialized lending and underwriting securities. As of February 28, 1999, the consolidated net worth of the private sector financial institutions in Brazil was R$52.2 billion.

Regulation by Central Bank

The Central Bank is authorized to implement the currency and credit policies prescribed by the CMN and to supervise all financial institutions. Any amendment to a financial institution's by-laws, increase in its capital or establishment or transfer of its principal place of business or any branch (whether in Brazil or abroad) must be approved by the Central Bank, which is also responsible for determining the minimum capital requirements for financial institutions. The Central Bank is responsible for ensuring that the accounting and statistical requirements established by the CMN are observed. Financial institutions must submit semi-annual financial statements reviewed by each institution's independent auditors and a formal audit opinion, as well as monthly unaudited financial statements prepared in accordance with the standard accounting rules promulgated by the Central Bank. As part of the Central Bank's supervision of their activities, financial institutions are required to make full disclosure of credit transactions, foreign exchange transactions, the destination of proceeds raised from export and import transactions, and any other related economic activity. Such data are usually supplied to the Central Bank on a daily basis through computer systems, reports and statements. The Central Bank also supervises the operations of consumer credit companies, securities dealers, stock brokerage companies, leasing companies, savings and loan associations and real-estate credit companies. See "—General" and "The Brazilian Economy—Changes in the Relationship between the Federal and Local Governments".

Central Bank regulations impose capital adequacy, liquidity, savings deposit insurance, and loan loss reserve requirements on regulated financial institutions.

Capital Adequacy, Liquidity and Concentration Limits. Since January 1, 1995, Brazilian financial institutions have been required to comply with the Basle Accord on risk-based capital adequacy, modified as described below by Resolution No. 2,099, dated August 17, 1994.

In general, the Basle Accord requires banks to maintain a ratio of capital to assets and certain off-balance sheet items, determined on a risk-weighted basis, of at least 11% for credit operations until December 31, 1998 and 20% for swap transactions. For margin deposits, guaranteed notes and premiums paid in ordinary operations of investment funds and fixed-income funds, the ratio required to be maintained is 5% of the net worth of the institution when such transactions have an aggregate value less than or equal to 100% of such net worth, 20% of such net worth when such transactions have an aggregate value of more than 100% but less than 300% of such net worth and 50% of such net worth when such transactions have an aggregate value of more than 300% of such net worth. At least half of the required capital must consist of Tier 1 capital, and the balance must consist of Tier 2 capital. Tier 1, or core, capital includes equity capital (*i.e.*, common shares and non-cumulative permanent preferred shares), share premium, retained earnings and certain disclosed reserves less goodwill. Tier 2, or supplementary, capital includes "hidden" reserves, asset revaluation reserves, general loan loss reserves, subordinated debt and other quasi-equity capital instruments (such as cumulative preferred shares, long-term preferred shares and mandatory convertible debt instruments). Tier 2 capital is limited to the total of a bank's Tier 1 capital. There are also limitations on the maximum amount of certain Tier 2 capital items. To assess the capital adequacy of banks under the risk-based capital adequacy guidelines, a bank's capital is evaluated on the basis of the aggregate amount of its assets and off-balance sheet exposure, which are weighted according to four broad categories of risk. The risk-based capital adequacy guidelines also establish credit conversion formulae for determining the credit risk of off-balance sheet items, such as financial guarantees, letters of credit and foreign currency and interest rate contracts.

Under Brazilian modifications to the Basle requirements (a) only Tier 1 capital (as modified with respect to revaluation reserves) may be counted towards the 11% minimum capital requirement, and (b) the risk weights assigned to certain assets and credit conversion amounts differ to a minor extent. Brazilian financial institutions may elect to calculate their capital requirements on either a consolidated or unconsolidated basis. As of November 30, 1998, the average ratio of capital to assets and certain off-balance sheet items (determined in accordance with the Basle Accord) of certain representative Brazilian banks was 28%, which exceeded the Basle requirements.

The Central Bank prohibits Brazilian multiple-service banks from holding, on a consolidated basis, permanent assets in excess of 90% of their adjusted stockholders' equity. The 90% threshold was reduced to 80% effective June 30, 1998; it will be further reduced to (a) 70% as of June 30, 2000; and (b) 60% as of June 30, 2002. Permanent assets include investments in subsidiaries as well as premises, equipment and intangible assets.

Until March 1998, each financial institution was prohibited from extending loans or advances or granting guarantees to a single borrower that, in the aggregate, exceeded 30% of that institution's shareholders' equity. Resolution No. 2,474 dated March 26, 1998 of the National Monetary Council of Brazil ("Resolution No. 2,474") reduced to 25% the cap on extensions of credit to a single borrower. Extensions of credit include, among other things, loans, advances, leasing operations and guarantees. Resolution No. 2,474 also corrects a distortion under prior regulations by including within the category of extensions of credit the purchase of debt securities issued by the borrower. Federal Government debt securities and certain debentures issued by leasing companies are excluded from the application of Resolution No. 2,474. Financial institutions will have until December 31, 2001 to comply with Resolution No. 2,474.

On May 7, 1998, the National Monetary Council of Brazil promulgated Resolution No. 2,493, which provides for the formation of special purpose companies to acquire receivables and issue debt securities backed by such receivables. The Government believes that through the securitization of receivables, banks will be better able to control credit risk through the sale of assets. The Government also anticipates that the involvement of credit rating agencies and bond insurance agencies in the underwriting process may lead to more stringent loan standards, thereby reducing systemic risks in the financial system.

Resolution No. 2,561 dated November 5, 1998 of the National Monetary Council of Brazil provides for the assignment of loans and certain other extensions of credit without recourse and prohibits the repurchase of the assigned credits. The measure is intended to discourage institutions from pursuing an aggressive loan policy simply because they are able to sell the credits to third parties. By a separate resolution, however, the National Monetary Council preserved the possibility of recourse to an assignor of mortgages in the context of mortgage-backed securitizations.

Deposit Insurance. On November 16, 1995, the Government implemented a deposit insurance system in Brazil, by creating the FGC to protect certain creditors in cases of (1) intervention, nonjudicial liquidation or bankruptcy of an institution or (2) the Central Bank's recognition of a state of insolvency at an institution that, according to current law, is not subject to one of the mechanisms listed in (1) above. Such insurance became effective in February 1996.

The participants in the FGC are all financial institutions and savings and loan associations, with the exception of credit cooperatives and the credit sections of cooperatives. The participating institutions make a monthly contribution of 0.025% of the total reported value of covered liabilities.

The following liabilities are covered by the guaranty provided by the FGC: demand deposits or those that may be withdrawn through prior notification; savings deposits; time deposits, in both book entry and certificated form; bills of exchange; real estate bonds; and mortgage bonds.

The following liabilities are not covered by the guaranty: liabilities in the name of other institutions that are members of the National Financial System; deposits, loans or any other resources contracted or raised abroad; and credits in the name of certain persons affiliated with an institution, generally managers and other members of the consolidated group of which such institution is a member.

The FGC is a nonprofit, civil association governed by private law, its bylaws and applicable legal and regulatory provisions. The FGC is headquartered in, and subject to the jurisdiction of, the municipality of São Paulo and its duration is unlimited.

The FGC guaranty covers up to R$20,000 per person of covered claims against a single institution or against all the institutions of a single financial conglomerate. Since February 1996, Brazilian banks have made monthly contributions to the FGC, which totalled R$2.6 billion on December 31, 1998.

Loan Loss Reserves. Under Central Bank regulations, secured and unsecured credits in local currency may remain in default for 60 days. After 60 days, unsecured credits must be classified as nonperforming and be fully provisioned, partially secured credits may remain in arrears for a maximum period of 180 days, and fully secured credits may remain in arrears for a maximum period of 360 days before being fully provisioned. Upon becoming 60 days in arrears, partially secured credits must be provisioned as to 50% of the recorded value of the credit and fully secured credits must be provisioned as to 20% of the recorded value of the credit. Further provisioning is required to be made every 30 days thereafter (up to the 180th day or, as the case may be, the 360th day) to ensure that the provision remains at the required level of 50% or, as the case may be, 20% of the recorded value of the loan. Loans made by financial institutions to public-sector borrowers are treated the same as loans to private-sector borrowers for this purpose. Credits in connection with import and export financing may remain in default for 30 days before being classified as nonperforming and fully provisioned.

Upon the bankruptcy of a borrower, credits are required to be provisioned in an amount equal to 100% of the recorded value of the credit.

At the time a loan loss provision is established, the entire loan is classified as non-performing. However, because a partial loan loss provision may be made under the circumstances described above, while the entire loan would be classified as nonperforming loans, a bank's nonperforming loans may exceed loan loss reserves, and the ratio of non performing loans to total loans may exceed the ratio of loan reserves to total loans.

Since January 1, 1996 and the abolition of the Central Bank requirement that financial statements be monetarily corrected, the outstanding principal balances of defaulted loans have not been indexed and, beyond 120 days, interest may only be recognized as income when effectively received. Credits that are in default and no longer considered to be recoverable must be written off after the end of the 180-day period during which they were classified as overdue.

On May 2, 1997, the National Monetary Council approved Resolution No. 2 390, which created a new credit risk system that is intended to strengthen the Central Bank's supervisory activities and improve the assessment of the credit risk by the banking system. Since June 30, 1997, financial institutions (including those under the administration of the Central Bank) have been required to submit reports to the Central Bank setting forth, for each client, in descending order, the amount of credit extended to such client (including credits in arrears or in liquidation) and liabilities of the financial institutions relating to such client (including co-obligor arrangements and guarantees) to the extent that the aggregate amount of such credits and liabilities exceeds R$50,000. Credits and liabilities in an aggregate amount less than R$50,000 relating to any client are to be reported on an aggregate basis, broken down by type of client (natural persons or juridical entities). The information collected is to be used by the Supervision Department of the Central Bank to refine its criteria for the classification of debtors by risk categories and for the assessment of provisions for nonperforming loans.

Foreign Currency Loans. Financial institutions in Brazil are permitted to borrow foreign currency-denominated funds in the international markets (either through direct loans or through the issuance of debt securities) for the specific purpose of on-lending such funds in Brazil to Brazilian corporations and financial institutions ("Foreign On-lendings"). These on-lendings take the form of loans denominated in Brazilian currency and indexed to the U.S. dollar. At the date hereof, Central Bank regulations establish a minimum term for borrowings of foreign currency-denominated funds of three years and exempt from income taxes the payment of interest on debt securities with maturities of more than eight years.

In addition, all proceeds from Foreign On-lendings that are not so lent to customers are subject to restrictions imposed by the Central Bank and generally may only be used for investments in government securities and deposits with the Central Bank.

Independent Accountants. Financial institutions are required to replace their independent accountants no later than every fourth fiscal year. A former independent accountant of a financial institution can be re-hired only after three complete fiscal years have elapsed from his prior engagement by such financial institution. Independent accountants are required to prepare the following reports: (i) a report on the examined audited financial statements with respect to compliance with accounting principles as well as the relevant rules issued by the CMN and the Central Bank; (ii) a report evaluating the quality and adequacy of internal control procedures, including risk assessment criteria and data processing systems; and (iii) a report on the compliance with applicable operational laws and regulations.

Each independent accountant is required to immediately communicate to the Central Bank any event that may materially adversely affected the relevant financial institution's status. Financial institutions are required to appoint an executive officer to a supervisory role in the area of accounting in order to ensure compliance with auditing and accounting rules and the rendering of accurate information.

Foreign Banks and Insurance Companies. Under current law, foreign banks duly authorized to operate in Brazil through a branch or a subsidiary are subject to the same rules, regulations and requirements applied to any other Brazilian financial institution. On February 26, 1999, there were 60 foreign-controlled or foreign-affiliated banks and 17 banks in which there was significant foreign participation operating in Brazil. In accordance with the Constitution, authorization for the establishment of new foreign financial institutions in Brazil is to be regulated by the Congress although to date no law has yet been enacted. Until the adoption of the law, the establishment in Brazil of new agencies, subsidiaries or branches of foreign financial institutions and any increase in a foreigner's percentage participation in existing institutions in the Brazilian financial system is prohibited, except when it results from international agreements or an express Presidential finding of public interest. The Government has expressed its intention to allow foreign investors to participate in the privatization of financial institutions, in accordance with Explanation (*"Exposicão de Motivos"*) No. 89, dated March 7, 1995 from the Minister of Finance to the President. Similarly, Explanation No. 190, dated May 14, 1996, indicates that the Government has an interest in promoting the participation of foreign capital in the health insurance system in order to encourage competition and ultimately expand insurance coverage at reduced cost to the customer.

In January 1997, the National Monetary Council initiated several measures aimed at liberalizing foreign investment in the financial sector and permitting foreign stock ownership and control of banks in Brazil. In 1998, foreign banks acquired control of 42 financial institutions in Brazil, including 15 banks. Between 1996 and 1998, foreign participation in the Brazilian financial system's total assets increased to 13% from 9%, and foreign participation in the Brazilian financial system's net worth increased to 14% from 9%.

Securities Markets

The CVM implements the policies of the CMN relating to the organization and operation of the securities industry. The CVM is responsible for regulating the country's stock exchanges, protecting investors and shareholders against fraud or manipulation with respect to any securities traded on the stock exchanges and promulgating accounting and reporting rules to ensure the availability to the public of information on the securities being traded and the companies issuing them. The Central Bank has licensing authority over brokerage firms and dealers and controls foreign investment and foreign exchange transactions.

Of Brazil's nine stock exchanges, the São Paulo Stock Exchange (*Bolsa de Valores de São Paulo* or "BOVESPA") and the Rio de Janeiro Stock Exchange (*Bolsa de Valores do Rio de Janeiro* or "BVRJ") are the most significant, accounting together in 1998 for approximately 98% of the daily trading activity. In both stock exchanges, trades are effected through both the floor bidding and electronic systems. On BVRJ, electronic trades are effected through the National Electronic Trading System ("SENN"), a computerized system inaugurated in 1991, which links the Rio de Janeiro Stock Exchange electronically with seven small regional exchanges. On BOVESPA, trades are effected through the Electronic Trading System introduced in 1990, linking brokerage firms throughout the country with BOVESPA.

In response to volatility in the Brazilian stock markets during the latter half of October 1997, BOVESPA and the Rio de Janeiro Stock Exchange implemented circuit breakers designed to halt trading when their respective stock indices fell by more than 10%. Such circuit breakers were triggered at various times in late October and early November 1997.

A company that is qualified to trade on one Brazilian stock exchange may qualify for trading on any other Brazilian stock exchange. At December 31, 1998, there were 527 companies listed on BOVESPA, the largest stock exchange in Brazil by average daily trading volume, and the aggregate market capitalization of all listed companies was approximately $160.9 billion. As of December 31, 1998, the aggregate trading volume on BOVESPA was approximately $7.6 billion, and six of the twenty companies with the largest capitalization listed on the stock exchanges in Brazil were controlled by the Government. Trades in securities listed on the Brazilian stock exchanges may be effected off the exchanges in certain circumstances, although the volume of such trading is limited. The table below sets forth some indicators of market activity on BOVESPA in the five years ended December 31, 1998:

Table No. 26

Market Activity on BOVESPA

	1994	1995	1996	1997	1998
Number of Listed Companies..	544	543	550	536	527
Market Capitalization(1)	189,058.18	147,567.57	216,927.18	255,409.31	160,886.69
Market Volume(1)	88,205.75	69,446.96	97,761.56	191,091.67	139,970.56

(1) In millions of U.S. dollars.
Source: BOVESPA

The Brazilian equity market is one of Latin America's largest in terms of market capitalization. The value of average daily trading volume increased from R$231 million in 1994 to R$260 million in 1995, R$397 million in 1996 and R$829 million in 1997. The average daily trading volume fell to R$658 million in 1998.

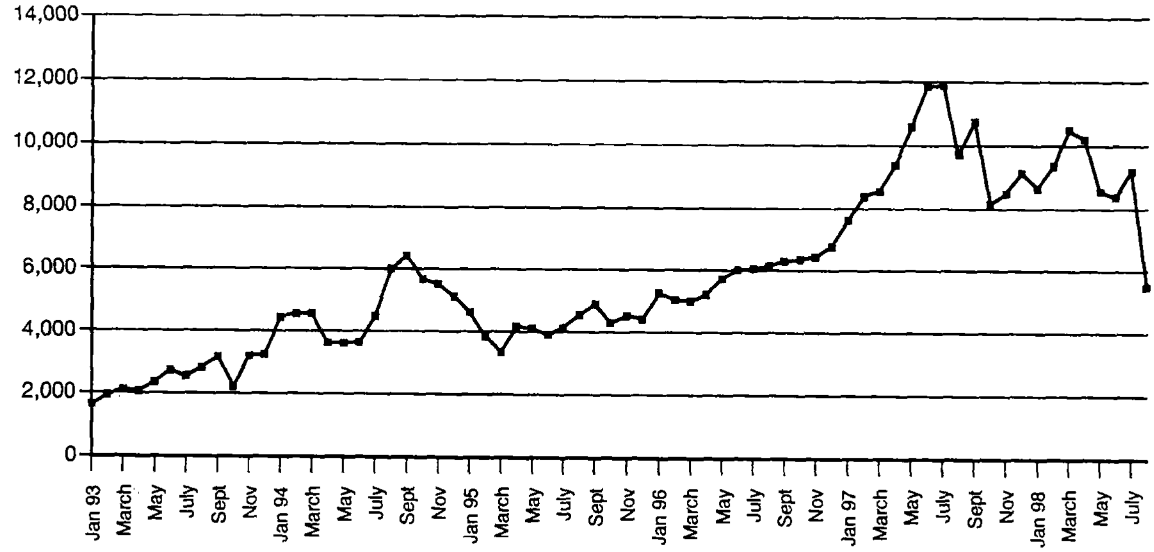
Trading on Brazilian stock exchanges by non-residents of Brazil is subject to specific rules under Brazilian foreign investment legislation. See "Balance of Payments and Foreign Trade—Foreign Investment".

In 1991, the Brazilian authorities created a mechanism (referred to as Annex IV) permitting foreign institutional investors to invest in the Brazilian stock exchanges through portfolios managed by Brazilian fund managers. Foreign capital invested in the Brazilian securities markets represents an increasingly important share of total capital in the stock exchanges. Foreign investor participation in BOVESPA increased from $5.5 billion in 1993 to $10.9 billion in 1994, $11.5 billion in 1995, $28.0 billion in 1996 and $49.5 billion in 1997. Although the foreign participation in BOVESPA declined in February 1995 to 14.9% from 27.5% in January 1995, in part due to the effects of the Mexican liquidity crisis in December 1994, foreign participation returned to levels between 28.4% and 32.1% during the second half of 1995. In December 1996, it reached 38.2%, but it subsequently declined to 25.0% in December 1998. The Government has sought to regulate the flow of foreign portfolio investment from time to time by varying the level of IOF taxation on Annex IV inflows; the maximum level of IOF taxation the Government currently has authority to impose on such inflows is 25%. See "Balance of Payments and Foreign Trade—Foreign Investment".

The Brazilian equity market is characterized by significant short-term price volatility. The closing levels (U.S. dollar adjusted) for the IBOVESPA, an index maintained by BOVESPA, were 407 at December 31, 1990, 1,581 at December 31, 1991, 1,523 at December 31, 1992, 3,217 at December 31, 1993, 5,134 at December 31, 1994, 4,420 at December 31, 1995, 6,773 at December 31, 1996, 9,133 at December 31, 1997 and 5,615 at December 31, 1998. The following chart sets forth the level of the IBOVESPA at the close of each of the months indicated since January 1993:

Price Graph for IBOVESPA—BOVESPA Stock Index (in dollars)

Range 1/31/93—8/31/98



PUBLIC FINANCE

Consolidated Public Sector Fiscal Performance

The consolidated public sector account is comprised of the accounts of the federal Government, public sector enterprises, and State and local governments. In turn, the federal Government account consolidates the accounts of the National Treasury, the social security system, and the income and loss statement of the Central Bank, but does not reflect the proceeds from privatizations. With the adoption of several important structural reforms in recent years, the Government has established as its objective a substantial improvement in the fiscal performance of the consolidated public sector as measured by the operational balance. In 1995, 1996, 1997 and 1998, however, the public sector recorded operational deficits of 4.9%, 3.8%, 4.3% and 7.5%, of GDP, respectively, compared to an operational surplus of 1.3% of GDP in 1994.

Brazil reports its fiscal balance using three principal measures, all of which are calculated according to the official statistical guidelines of the IMF:

- *Financial Balance, or Nominal Balance*, which when in deficit is referred to as the Public Sector Borrowing Requirement ("PSBR"), is calculated as the difference between the debt in one period and the consolidated public sector debt in the previous period, excluding the effects of the Government's privatization program;
- *Primary Balance*, which is the financial balance less net borrowing costs of the Government; and
- *Operational Balance*, which excludes the inflationary component of interest payments on domestic debt of the non-financial public sector. This measure is calculated by adding to the primary balance accrued real interest on external and domestic debt. The operational balance is used to correct the distortions which affect the measurement of public finances in an inflationary environment.

The PSBR increased from 29.6% to 59.1% of GDP between 1990 and 1993 before decreasing to 45.5% in 1994. The increase reflected in part a significant increase in the nominal deficit of the State and local governments (from 8.5% of GDP in 1990 to 24.9% of GDP in 1993 before declining to 19.4% of GDP in 1994). In addition, the federal Government experienced an increase in its PSBR from 12.3% of GDP in 1990 to 20.7% of GDP in 1993, although it moderated to 17.8% of GDP in 1994. In 1995, a year of significantly lower inflation than in prior years, the PSBR reached 7.2% of GDP. The PSBR declined to 5.9% in 1996, with the nominal deficits of the federal Government, the State and local governments and the public sector enterprises amounting to 2.6%, 2.7% and 0.6%, respectively, of GDP. In 1997, the PSBR rose slightly to 6.1% of GDP, and the nominal deficits of the federal Government, the State and local governments and the public sector enterprises amounted to 2.6%, 3.0% and 0.5%, respectively, of GDP. In 1998, the nominal deficit of the federal Government increased significantly to 5.5% of GDP from 2.6% of GDP in 1997, resulting in a PSBR of 8.0% of GDP in 1998. The nominal deficit of the State and local governments, by contrast, dropped to 2.0% of GDP in 1998 from 3.0% of GDP in 1997, while the nominal deficit of public sector remained constant at 0.5% of GDP in 1998.

Brazil generated a consolidated primary surplus in each year from 1990 to 1995. During 1992, Brazil had a primary surplus of 2.3% of GDP. However, real interest expense (both domestic and external) on the public debt for 1992 totalled 4.5% of GDP, leading to an operational deficit of 2.2% of GDP for that year. As a result of implementation of structural reforms, the consolidated primary surplus improved to 2.6% of GDP in 1993. In addition, the real interest expense on the public debt declined to 2.4% of GDP, resulting in an operational surplus of 0.2% of GDP. Individual operational results improved to 0.0% for both the federal Government and the public sector enterprises, and a surplus of 0.2% at the State and local levels.

In 1994, the consolidated primary surplus increased to 5.3% of GDP, and the real interest expense on the public debt increased to 4.1% of GDP. Consequently, Brazil posted a consolidated operational surplus of 1.4% of GDP in 1994. In 1994, the federal Government, State and local government and public sector enterprises posted an operational surplus of 1.6%, an operational deficit of 0.6%, and an operational surplus of 0.3%, respectively, of GDP. In 1995, the consolidated primary surplus declined significantly to 0.4% of GDP, with the real interest expense on the public debt amounting to 5.3% of GDP. As a result, the public accounts showed a consolidated operational deficit of 4.9% of GDP, of which the federal Government, State and local government and public sector enterprises accounted for 1.7%, 2.3% and 0.9%, respectively, of GDP.

In 1996, the consolidated primary balance showed a deficit of 0.1% of GDP, largely because of a State and local government primary deficit equivalent to 0.6% of GDP; during the same period, the federal Government and public sector enterprises showed primary surpluses of 0.4% and 0.1%, respectively. During that year, the real interest expense on the public debt fell to 3.7% of GDP. As a result, the consolidated operational deficit fell to 3.8% of GDP, of which 1.6%, 1.9% and 0.3% were attributable to the federal Government, State and local government and public sector enterprises, respectively.

The consolidated primary deficit increased to 0.9% of GDP in 1997 as the primary balance of the federal Government went from a surplus of 0.4% of GDP in 1996 to a deficit of 0.3% of GDP in 1997, largely as a result of a deficit in social security equivalent to 0.8% of GDP. The primary balance of the State and local governments and the public sector enterprises remained largely unchanged from the previous year, with the State and local governments showing a primary deficit of 0.7% of GDP in 1997 and the public sector enterprises registering a primary surplus of 0.1% of GDP. The real interest expense on the public debt continued to fall in 1997 to 3.3% of GDP. However, the consolidated operational deficit rose to 4.3% of GDP, of which 1.8%, 2.3% and 0.3% were attributable to the federal Government, State and local governments, and public sector enterprises, respectively.

In 1998, the consolidated primary result was 0.0% of GDP, versus a deficit of 0.9% of GDP in 1997. The improvement in the consolidated primary result was largely attributable to the primary result of the federal Government, which moved from a deficit of 0.3% of GDP in 1997 to a surplus of 0.6% of GDP in 1998. The primary result of the State and local governments also showed improvement, but still ended 1998 with a deficit of 0.2% of GDP. The primary result of the public sector enterprises, by contrast, moved from a surplus of 0.1% of GDP in 1997 to a deficit of 0.4% of GDP in 1998. The consolidated operational deficit increased significantly to 7.5% of GDP in 1998 from 4.3% of GDP in 1997, reflecting a real interest expense that more than doubled as a percentage of GDP to 7.6% of GDP in 1998 from 3.3% of GDP in 1997. The operational result of the federal Government was most affected by the increase in real interest expense; the federal Government ended 1998 with an operational deficit of 5.2% of GDP versus its operational deficit of 1.8% of GDP in 1997.

The ability of the Government to achieve economic growth targets depends in part on containing public expenditure in order to reduce the public sector borrowing requirement and facilitate private sector investment. Among the measures the Government has indicated would contribute to the reduction of public sector fiscal deficit are (i) not indexing increases in the minimum wage or in public sector wages to past inflation, (ii) maintaining interest rates at lower levels, thereby reducing the cost of servicing the public debt, and (iii) encouraging the structural adjustment of the States. See "The Brazilian Economy—*Plano Real* and Current Economic Policy", "—Salaries and Wages", and "—Changes in the Relationship between the Federal and Local Governments".

Set forth below are the public sector borrowing requirements since 1994. In addition to the cash balance of the National Treasury, the public sector borrowing requirements include the borrowing requirements of public sector enterprises, the social security system, the Central Bank, States and municipalities and certain public funds.

Table No. 27

Public Sector Borrowing Requirements Historical Summary(1)

	1994	1995	1996	1997	1998
Selected Economic Indicators(2)					
Real GDP Growth (Decline)	5.9%	4.2%	2.7%	3.6%	(0.1)%
Monetary Base (end of period) change	3,322.4	22.6	(8.7)	60.8	23.1
Real interest rate(3)	24.2	33.4	16.5	16.1	26.6
Implicit interest rate(4)	16.3	27.9	13.7	12.1	12.1
Public Finance(5)					
Financial result	(45.5)%	(7.2)%	(5.9)%	(6.1)%	(8.0)%
Primary result	5.3	0.4	(0.1)	(1.0)	0.0
Real interest	(4.1)	(5.3)	(3.7)	(3.3)	(7.6)
Domestic	(3.5)	(4.7)	(3.2)	(3.0)	(7.3)
External	(0.6)	(0.5)	(0.5)	(0.3)	(0.3)
Operational result	1.1	(5.0)	(3.8)	(4.3)	(7.5)
Domestic financing	4.9	(6.4)	(4.9)	(2.2)	(4.4)
External financing	1.2	2.0	0.9	(0.7)	(2.2)
Issue of money	(4.3)	(0.6)	0.2	(1.4)	(0.8)

(1) Surplus (deficit).
(2) Accumulated change from prior period.
(3) Accumulated change in the fiscal year, deflated by the GPI-DS.
(4) Implicit real interest rate on public sector internal debt of the fiscal year.
(5) All figures expressed as a percentage of GDP.
Source: Central Bank

The table below shows the contributions of the federal Government, the State and local governments and public sector enterprises with regard to the PSBR.

Table No. 28

Public Sector Borrowing Requirements(1)(2) by Secto

Item	% of GDP 1994(3)	% of GDP 1995(3)	% of GDP 1996(3)	% of GDP 1997(3)	% of GDP 1998(3)
Total					
Financial	(45.5)%	(7.2)%	(5.9)%	(6.1)%	(8.0)%
Primary	5.3	0.4	(0.1)	(1.0)	0.0
Operational	1.4	(4.9)	(3.8)	(4.3)	(7.5)
Federal Government					
Financial	(17.8)	(2.3)	(2.6)	(2.6)	(5.5)
Primary	3.2	0.6	0.4	(0.3)	0.6
Operational	1.6	(1.7)	(1.6)	(1.8)	(5.2)
State and Local Government					
Financial	(19.3)	(3.6)	(2.7)	(3.0)	(2.0)
Primary	0.9	(0.2)	(0.6)	(0.7)	(0.2)
Operational	(0.6)	(2.3)	(1.8)	(2.3)	(1.8)
Public Sector Enterprises					
Financial	(8.3)	(1.3)	(0.6)	(0.5)	(0.5)
Primary	1.2	0.1	0.1	0.1	(0.4)
Operational	0.3	(0.9)	(0.3)	(0.3)	(0.5)

(1) Amounts calculated using the GPI-DS adjusted as of month-end.
(2) Surplus (deficit).
(3) Reflects the ratio of flows to GDP, both valued for the last month of the period, using GPI-DS.
Source: Central Bank

Budget Process

The Government's fiscal year is the calendar year. Responsibility for preparation of the federal budget rests with the executive branch, although the National Congress plays a major role in budget determinations. Based on discussions among representatives from the National Treasury of the Ministry of Finance and the Secretariat of Planning, Budget and Coordination ("Seplan"), Seplan prepares a budget proposal. After discussions among representatives of Seplan, the Treasury and each other Ministry, Seplan submits a formal proposal for the *Lei de Diretrizes Orçamentárias* (the budget directives law or "LDO") for the succeeding fiscal year to the President of the Republic. The President, in turn, submits the LDO proposal, with any revisions, to the National Congress. The LDO proposal with respect to the succeeding year must be submitted to Congress by April 15.

Congress may revise the LDO proposed by the President. Congress is charged by law to submit to the President the LDO as revised by June 30 and may not begin its winter recess until it does so. The LDO becomes effective immediately if Congress approves the presidential proposal without revision. If Congress alters any item of the proposal, the President may veto any provision of the revised LDO. All provisions that are not vetoed become effective upon presidential signature. Congress may override the veto by a two-thirds majority vote. If the veto is overridden, the provision becomes effective upon the override.

The executive branch is charged with submitting to Congress a detailed budget for the succeeding fiscal year that is consistent with the broad contours set forth in the LDO. Each ministry proposes a detailed budget with respect to its operations, and Seplan meets with each ministry to discuss its proposal. Seplan finalizes a federal budget proposal, which it submits to the President. The President is then required to submit the budget, as revised, to Congress by August 31.

Congress may revise some items in the President's proposed budget. Congress may not, however, alter the items regarding payments on any external debt that the Republic has incurred. By December 15, Congress must submit to the President the budget, as revised, for the succeeding year.

The President is granted fifteen days to review and sign the budget. If the President signs the budget or a veto is overridden prior to the end of the year, the provisions that are not vetoed or for which the veto has been overridden become effective as of January 1 of the next year. After presidential signature, implementing decrees authorizing expenditures are generally issued within five to ten days, but certain expenditures are permitted to be made immediately.

The budgets for recent years, including years 1990 through 1999, have not been finally approved prior to January 1 of the year. In order to avoid a shutdown of the Government, the LDO typically authorizes the Government to use each month an amount equivalent to one-twelfth of the proposed annual expenditure included in the Government's proposed budget pending before Congress. Exceptions to this rule have been made in accordance with a provision of the LDO and through the issuance of provisional measures.

1999 Budget

The 1999 budget bill was approved by the National Congress and signed by the President on February 23, 1999.

The budget predicts an operational surplus of R$16.3 billion (1.80% of GDP) based on estimated expenditures and revenues of R$183.6 billion and R$199.9 billion, respectively.

The principal assumptions underlying the 1999 budget estimates are set forth below:

Table No. 29

Principal 1999 Budget Assumptions

	Year Ended December 31, 1999
Gross Domestic Product	
GDP Nominal (billions of dollars)	$907.9
Real GDP Growth	(1.0)%
Inflation	
Domestic Inflation (GPI-DS)	2.0 %

Source: SEPLAN/Federal Budget Secretariat (SOF)

The following table sets forth revenues and expenditures of the Government from 1993 through 1997 and as projected in the 1998 budget.

Table No. 30

Primary Result of the Central Government and 1999 Budget(1)

	Year Ended December 31,		
	1997	1998	1999 Budget
	(in millions of *reais*)		
1—Total Revenues	**160,250**	**183,892**	**207,406**
1.1—Treasury revenue	115,990	137,677	157,696
1.1.1—Administrative revenue	107,119	117,775	134,315
1.1.2—Refunds	(2,826)	(3,540)	0
1.1.3—Direct taxes	7,307	7,432	5,551
1.1.4—Other revenues	5,138	16,776	17,830
1.1.5—Fiscal incentives	(748)	(766)	0
1.2—Social security receipts	44,260	46,215	49,710
2—Total Expenditures	**157,797**	**178,358**	**191,445**
2.1—Treasury expenditures	110,746	124,986	131,245
2.1.1—Transfers to States and municipalities	23,488	27,217	31,192
2.1.2—Expenditures of the Federal Administration	84,578	94,846	97,252
2.1.3—Subsidies and subventions	2.680	2,923	2,801
2.2—Social security benefits	47,051	53,372	60,200
3—Primary Result(3)	**1,758**	**5,384**	**15,961**
3.1—Federal Government result (1-2)	2,453	5,534	16,161
3.1.1—National Treasury (1.1-2.1)	5,244	12,691	26,451
3.1.2—Social security (1.2-2.2)	(2,791)	(7,157)	(10,490)
3.2—Central Bank result	(695)	(150)	0
4—Financing Requirement(4)	**2,886**	**(5,024)**	**n.a.**
5—Errors and Omissions (3+4)	**(4,644)**	**(360)**	**n.a.**

(1) Consolidated accounts of the National Treasury, Social Security and the Central Bank.
(2) Exchange rates: 1997=R$1.081/$1; 1998=R$1.1611/$1 and 1999=R$1.7020/$1 (rate of March 31, 1999).
(3) Above the line. Surplus/(deficit).
(4) (Surplus)/deficit.

Source: Ministry of Finance/National Treasury Secretariat and Central Bank

The following table sets forth the expenditures of the Government in the years indicated, by function. The figures in this table are not directly comparable with those set forth in the table above entitled "Primary Result of the Central Government and 1999 Budget", because the expenditures set forth in the table above were calculated in accordance with the IMF concept therefor, which does not include, among other things, debt service expenditures and certain financial investments.

Table No. 31

Expenditures of the National Treasury by Function

Itemization	1994	1995	1996	1997	1998	1999(3) Budget
			(in millions of dollars)(1)			
Legislative	$ 724	$ 1,147	$ 1,231	$ 1,505	$ 1,331	$ 901
Judiciary	2,130	3,233	3,734	4,956	5,635	3,471
Administration and Planning	118,375	126,143	145,696	211,744	216,572	207,525
Agriculture	6,064	8,821	6,267	8,095	6,043	3,240
Communications	101	101	110	179	486	169
National Defense and Public Security	6,994	9,050	8,907	9,121	8,242	5,648
Regional Development	18,059	20,160	20,857	22,434	21,741	14,046
Education and Culture	8,932	10,210	9,446	9,667	12,318	8,827
Energy and Mineral Resources	490	527	633	802	765	575
Housing and Urban Planning	1,802	119	342	395	1,356	770
Industry, Commerce and Services	1,834	913	957	1,078	1,987	1,515
Foreign Affairs	527	412	425	410	391	234
Health and Sanitation	21,212	16,102	14,651	16,674	16,256	11,024
Labor	6,519	6,016	6,912	6,674	8,049	4,784
Assistance and Social Security	76,278	57,272	63,626	64,885	64,662	50,084
Transportation	3,172	2,593	2,919	3,466	4,094	3,167
Intergovernment Transfers	—	72,633	1,524	1,193	—	—
Contingency Reserve	—	—	—	—	1,387	616
Total(2)	$273,212	$335,453	$288,236	$363,277	$371,318	$316,597

(1) Converted to U.S. dollars using the annual average commercial exchange rate (sell side).

(2) Total expenditures in this table are those reflected in the accounts of the Ministry of Finance, which treats certain expenditures as having been incurred when committed even though the corresponding amounts are disbursed in a later year.

(3) Estimates. *Source: General Budget of the Republic—Secretariat of Budget and Finance.*

Source: Federal General Balance Sheet—Ministry of Finance

Taxation and Revenue Sharing Systems

The Constitution authorizes the levying and collection of taxes by the taxing authorities of federal, State and municipal governments, and mandates that the federal Government share most of its tax revenues with the States, municipalities and other institutions. The federal Government collects taxes on personal and corporate income, IPI, a rural property tax ("ITR"), IOF, certain mandatory contributions to the social security system from legal entities, employers and employees, and import and export tariffs. State authorities collect inheritance taxes, automobile property taxes and taxes on goods sold in or passing through that State ("ICMS"). Municipalities and the Federal District collect taxes on urban property, transfers of property rights and services.

Income Taxation. Significant changes to the Brazilian income taxation system were made in December 1995. For corporate and other legal entities: (i) the basic tax was reduced to 15% from 25%, while the surtax on taxable net income exceeding R$240,000 was reduced to 10% from previous levels of 12% and 18%; (ii) the tax related to social welfare levied on net profit was reduced to 8% from 10% with respect to enterprises in general, and to 18% from 30% in the case of financial institutions; (iii) the deductions related to benefits granted to employees were prohibited in the calculation of taxable net income; (iv) only operating expenses directly related to the business of the enterprise are allowed to be deducted; (v) with respect to profits earned by foreigners, the tax levied on passive investment income increased to 15% from 10%; taxes on capital gains and loan interest were reduced to 15% from 25%; profits from operations and dividends were exempted from taxation as were gains attributable to the increase in market value of traded securities, consistent with rules applicable to Brazilian citizens; (vi) income earned by Brazilian enterprises abroad are included in the calculation of taxable income of the enterprise in Brazil, and taxes paid abroad are credited toward the tax paid in Brazil; and (vii) the tax levied on the nominal yield from financial investments in fixed income was increased to 15% from 10%, while variable income is taxed at the rate of 10%.

For individual taxpayers, the maximum rate of income taxation was reduced from 35% to 25%. Included in the Government's November 1997 fiscal package, however, was a measure that raised the maximum rate to 27.5%. See "The Brazilian Economy—*Plano Real* and Current Economic Policy". Deductions were allowed for certain contributions to private social security (but payments therefrom were includable) and income from the Brazilian government or its instrumentalities was made subject to taxation.

Value Added and Other Taxes. The federal value added tax on manufactured products is levied at scheduled rates at each stage of the production and distribution process. Import and export tariffs are based on published tariff schedules. See "The Brazilian Economy—Historical Background to Economic Policies".

The IOF, a tax imposed on the Brazilian currency equivalent of foreign currency entering Brazil, currently applies to investments in fixed-income funds at a rate of 2.0%. Prior to March 1995, the IOF had also been imposed on loans and investments in the stock market. On April 25, 1997, the Government announced revised rates for the IOF. The revised rates included (i) a 0% rate on foreign currency transactions relating to loans and issuances of debt securities, and investments in non-fixed income securities and privatization funds and (ii) a 2% rate on foreign currency transactions related to investments in fixed income investment funds, interbank transactions with institutions abroad and inflows of short-term funds from non-residents of Brazil. After increasing IOF rates in December 1998, the Government again reduced such rates to 0% for the transactions described in clause (i) and 0.5% for the transactions described in clause (ii). See "Balance of Payments and Foreign Trade—Foreign Investment". This tax does not apply to exchange transactions effected by the federal Government, States, municipalities, the Federal District or their foundations, autonomous government entities, or entities maintained by offshore international organizations. The IOF tax is also levied on domestic financial market transactions, including loans, gold, certain foreign exchange and securities transactions and insurance payments. Moreover, gains on certain financial transactions are also subject to taxation when the gain is realized and withdrawn from the financial system. Such gains are also included as taxable income for annual reporting purposes, and the transactions must be disclosed on the annual tax return.

On September 13, 1996, in a further effort to liberalize the export sector and to stimulate growth, the federal Government approved the elimination of the ICMS on exports of primary and semi-finished goods and on the acquisition of certain fixed assets. The federal Government intends to reimburse States for loss of ICMS revenues for periods ranging from 6 to 10 years. See "Balance of Payments and Foreign Trade—Foreign Trade".

Social Contributions. Business entities are required to make three "contributions" to social welfare funds. First, corporations must make a social contribution of 8% of monthly net profits. For financial institutions this contribution, which had been 18%, was initially increased retroactively to 30% for the period from January 1, 1996 to June 30, 1997 pursuant to Constitutional Amendment No. 10 of March 4, 1996. The required contribution for financial institutions was subsequently reduced to 18% effective January 1997. See "The Brazilian Economy—Constitutional Reform". Second, corporations (except financial institutions) must contribute 2.0% of monthly corporate billings to COFINS. Third, corporations must contribute 0.65% of billings to finance other social programs, including unemployment programs (known by their acronym, PIS/PASEP). Financial institutions must contribute 0.75% of gross operating revenue to PIS/PASEP. These contributions are turned over directly to the FEF and are not available for other general budgetary purposes. Other sources of funding for social programs include progressively graduated social security taxes that are shared by employers and their employees.

Revenue Sharing. The Constitution mandates the distribution to, or sharing with, the States, municipalities and regions of certain types of taxes collected by the federal Government. The municipalities are entitled to: (i) funds derived from withholding tax levied on payments made, in any way, by the municipalities, including autonomous entities and foundations thereof, (ii) 50.0% of the revenues from automobile property taxes, (iii) 25.0% of the ICMS, and (iv) 50.0% of the tax on rural property. The States are entitled to funds derived from withholding tax levied on payments made, in any way, by the States, including autonomous entities and foundations thereof.

The federal Government is required to transfer 47.0% of the proceeds from the IPI and the income tax as follows: (i) 21.5% to the States and Federal District Participation Funds, (ii) 22.5% to the Municipality Participation Fund and (iii) 3% to the financing programs for the productive sector in the North, Northeast and Central West Regions. The federal Government must transfer another 10.0% of the proceeds of the IPI to the States and Federal District ratably to their respective exports of manufactured products; the States must transfer 25.0% of these amounts to the municipalities.

All of the revenues derived from IOF levied on transactions in gold as a financial asset are distributed with 70.0% allocated to the municipalities and 30.0% allocated to the States, Federal District or federal territory of origin.

The federal Government must dedicate at least 18.0% of annual tax revenues to education, and the municipalities, States and Federal District must invest at least 25.0% of their annual revenues in this area.

The resources of the ESF created by Constitutional amendment for the 1994 and 1995 fiscal years were invested in health and education systems, social security benefits and ongoing social assistance services, including settling of social security debts and other relevant economic and social programs. The following tax revenues were allocated to the ESF: (i) funds derived from withholding tax levied on payments made, in any way, by the federal Government, including autonomous entities and foundations thereof, (ii) a portion of the funds attributable to the increase in the social contributions tax from 23% to 30% of the net profit of financial institutions, (iii) 5.6% of the total income tax collected, (iv) 20.0% of the revenues, net of transfers to States and municipalities, derived from federal Government taxes and contributions, with the exception of the portions mentioned in items (i), (ii) and (iii) above, (v) all the revenues obtained from PIS/PASEP contributions payable by financial institutions and (vi) other revenues provided for in specific laws. The FEF (which succeeded the ESF) was extended from June 30, 1997 to December 31, 1999 through the adoption on November 25, 1997 of Constitutional Amendment No. 17.

PUBLIC DEBT

General

Public sector debt in Brazil consists of the internal and external debt of the federal Government, State and local governments and public sector enterprises. Pursuant to the Constitution, the Brazilian Senate is vested with powers to establish, at the request of the President, (i) global limits for the consolidated debt of the federal Government, States and municipalities, (ii) the terms and conditions of the internal and external financial transactions of the Government, including public sector enterprises, at all levels of government, and (iii) the terms and conditions for guarantees of the federal Government of any internal or external financial transaction. In addition, all external financial transactions entered into at any level of government must be authorized by the Senate.

The aggregate amount of consolidated gross public sector debt more than doubled between 1993 and 1997, increasing in each year during that period from $203.6 billion in 1993 to $416.6 billion in 1997. Consolidated gross public sector debt initially declined as a percentage of GDP from 44.5% in 1993 to 41.4% in 1994 before increasing to 44.7% of GDP and 52.4% of GDP in 1995 and 1996, respectively. Consolidated gross public sector debt amounted to 52.0% of GDP in 1997. The growth in consolidated net public sector debt during this period was less marked, rising from $149.4 billion in 1993 to $276.6 billion in 1997, an 85.1% increase.

The substantial growth in the aggregate amount of consolidated gross public sector debt is attributable in large part to the large increase in the gross debt of the federal, State and local governments. The gross debt of the federal Government (including the Central Bank) increased by 202.5% between 1993 and 1997, from $122.8 billion in 1993 to $371.4 billion in 1997. After staying at roughly the same level in 1993 as in 1992, the gross debt of the federal Government increased significantly to $202.0 billion in 1994 from $122.8 billion in 1993, following the completion of the Republic's Brady Plan-type restructuring in April 1994 pursuant to which the Republic issued debt securities in exchange for, among other things, external debt of State and local governments and certain other public sector entities. See "—Debt Crisis and Restructuring—1992 Financing Plan". In 1995, 1996 and 1997, the gross debt of the federal Government increased to $243.2 billion (33.9% of GDP), $307.1 billion (40.8% of GDP) and $371.4 billion (46.4% of GDP), respectively. A large part of this increase is attributable to the issuance by the Government of domestic debt securities in an effort to regulate the monetary base. The real average rate of interest accumulated in the twelve-month period ended August 31, 1998 on such domestic securities was 23.0% as compared to 33.4% as of December 31, 1995. See "The Financial System—Monetary Policy and Money Supply".

The gross debt of the State and local governments increased by 147.7% between 1993 and 1997, from $43.0 billion in 1993 to $106.6 billion in 1997. The gross debt of the State and local governments also increased as a percentage of GDP during this period, from 9.4% of GDP in 1993 to 13.3% of GDP in 1997. The gross debt of the public sector enterprises, by contrast, declined significantly during the period, from $64.7 billion (14.1% of GDP) in 1993 to $34.4 billion in 1997 (4.3% of GDP), a 46.8% decrease.

At May 31, 1999, the Republic's net public sector debt stood at R$478.9 billion, or approximately 49.1% of GDP.

Since December 31, 1993, the debt profile of the Republic has been substantially altered due to the Brady Plan-type restructuring of Brazil's external debt in April 1994. Following that restructuring, the maturity profile of Brazil's public sector external debt was substantially lengthened, from an average of 6.9 years at December 31, 1993 to an average of 8.8 years at December 31, 1996. The average maturity of Brazil's public-sector external debt has declined in recent years, reaching 7.7 years at December 31, 1997 and 6.9 years at December 31, 1998. See "—Debt Crisis and Restructuring". In June 1997, the Republic completed an exchange offer pursuant to which the Republic acquired and cancelled approximately $2.7 billion aggregate outstanding principal amount of bonds issued in that restructuring. In addition, approximately $5.3 billion aggregate principal amount of Par Bonds that had been pledged to the Central Bank by Brazilian banks undergoing liquidation were cancelled in December 1997, following the sale of such Par Bonds to the National Treasury in exchange for National Treasury Notes. See "—Debt Crisis and Restructuring—1992 Financing Plan". After giving effect to such cancellations, approximately $35.8 billion aggregate principal amount of bonds issued pursuant to the Republic's Brady Plan-type restructuring remained outstanding on December 31, 1997. On December 31, 1998, annual debt service (principal and interest) on public sector external debt was equivalent to approximately $15.4 billion, which amounted to approximately 30.2% of receipts from exports of goods.

The following table sets forth the consolidated gross and net debt of the public sector for each of the periods indicated.

Table No. 32

Public Sector Debt

	1994	As a % of GDP	1995	As a % of GDP	1996	As a % of GDP	1997	As a % of GDP	1998	As a % of GDP
	(in millions of dollars, except percentages)									
Consolidated Gross Public										
Sector Debt*	$267,646	41.4%	$320,477	44.7%	$394,791	52.4%	$416,593	52.0%	$ 449,287	59.6%
Internal(1)	173,060	26.8	225,306	31.4	300,366	39.9	328,095	41.0	354,179	47.0
External(2)	94,586	14.6	95,171	13.3	94,426	12.6	88,498	11.1	95,109	12.6
By Sector										
Federal Government and										
Central Bank										
Gross Debt	$201,963	31.3%	$243,192	33.9%	$307,092	40.8%	$371,426	46.4%	$ 412,149	54.7%
Internal	121,668	18.8	163,124	22.8	230,957	30.7	301,904	37.7	333,788	44.2
Securities Debt	71,392	11.1	109,795	15.3	166,481	22.1	226,143	28.2	267,095	35.4
Other debt(3)	50,276	7.8	53,379	7.4	64,476	8.6	75,760	9.5	66,693	8.8
External	80,295	12.4	80,068	11.2	76,135	10.1	69,522	8.7	78,361	10.4
Credits	(123,958)	(19.2)	(150,133)	(20.9)	(183,451)	(24.4)	(221,065)	(27.6)	(220,686)	(29.2)
Internal	(82,100)	(12.7)	(94,474)	(13.2)	(119,522)	(15.9)	(167,219)	(20.9)	(174,457)	(23.1)
Public Sector(4)	(40,544)	(6.3)	(47,844)	(6.7)	(51,166)	(6.8)	(84,529)	(10.6)	(95,958)	(12.7)
Other(5)(6)	(41,556)	(6.4)	(46,830)	(6.5)	(68,357)	(9.1)	(82,690)	(10.3)	(78,499)	(10.4)
External(7)	(41,858)	(6.5)	(55,659)	(7.8)	(63,929)	(8.5)	(53,846)	(6.7)	(46,229)	(6.1)
State and Local Government										
Gross Debt	$ 62,674	9.7%	$ 77,401	10.8%	$ 92,453	12.3%	$106,579	13.3%	$ 111,274	14.8%
Internal	60,534	9.4	75,078	10.5	89,569	11.9	102,722	12.8	106,184	14.1
External	2,140	0.3	2,332	0.3	2,894	0.4	3,857	0.5	5,090	0.7
Credits	(2,140)	(0.3)	(2,808)	(0.4)	(2,584)	(0.3)	(2,587)	(0.3)	(2,900)	(0.4)
Internal	(2,140)	(0.3)	(2,808)	(0.4)	(2,584)	(0.3)	(2,587)	(0.3)	(2,900)	(0.4)%
Public Sector(8)(9)	0	0.0	0	0.0	0	0.0	0.0	0.0	0	0.0
Other(6)	(2,140)	(0.3)	(2,808)	(0.4)	(2,584)	(0.3)	(2,587)	(0.3)	(2,900)	(0.4)
External(7)	0	0.0	0	0.0	0	0.0	0.0	0.0	0	0.0
Public Sector Enterprises										
Gross Debt	$ 46,288	7.2%	$ 50,757	7.1%	$ 52,045	6.9%	$ 34,419	4.3%	$ 32,238	4.3%
Internal	34,137	5.3	37,988	5.3	36,649	4.9	19,300	2.4	20,580	2.7
External	12,151	1.9	12,771	1.8	15,396	2.0	15,119	1.9	11,658	1.5
Credits	(3,354)	(0.5)	(3,863)	(0.5)	(6,366)	(0.8)	(12,194)	(1.5)	(11,134)	(1.5)
Internal	(3,182)	(0.5)	(3,582)	(0.5)	(6,289)	(0.8)	(12,125)	(1.5)	(11,075)	(1.5)
Public Sector(10)	(2,735)	(0.4)	(3,038)	(0.4)	(5,634)	(0.7)	(11,301)	(1.4)	(10,416)	(1.4)
Others(6)(11)	(448)	(0.1)	(544)	(0.1)	(655)	(0.1)	(825)	(0.1)	(660)	(0.1)
External(12)	(172)	0.0	(281)	0.0	(77)	0.0	(69)	0.0	(59)	0.0
Net Public Sector Debt(13)	$181,473	28.1%	$214,576	29.9%	$259,189	34.4%	$276,576	34.5%	$ 321,771	42.6%
Internal	128,917	20.0	175,325	24.5	228,770	30.4	241,994	30.2	272,119	36.0
External	52,556	8.1	39,251	5.5	30,419	4.0	34,583	4.3	49,652	6.6

* Consolidated gross public sector debt, as presented in this table, does not consolidate debts between public sector entities. This table does not include liabilities related to the FCVS program. See "—Housing Compensation Fund for Salary Fluctuation (*Fundo de Compensação de Variações Salariais*)".

(1) Total domestic debt of Federal, State and local government less public sector internal credits.

(2) Total external debt of the Federal, State and local government, including short-term debt obligations.

(3) Includes monetary base, *cruzados novos* in accounts frozen under the Collor Plan, compulsory deposits required upon release of frozen accounts, other deposits of the financial system with the Central Bank and federal securities that can be used in the national privatization program. See "—Domestic Privatization Currencies".

(4) Debt of public enterprises owed to Banco do Brasil pursuant to Ministry of Finance Directive 30, debt securities issued by state and local governments, debt of States and municipalities issued under Resolution 8,727 of 1993 and credits from the Central Bank to state banks.

(5) Monetary reserves invested in overnight deposits, net banking debt, taxes receivable, social security, other accounts, FAT-BNDES and credits from the Central Bank to financial institutions.

(6) Other internal credits consist primarily of deposits at private sector financial institutions.

(7) External credits are equivalent to the federal Government's international reserves. The external credits of the federal Government and the Central Bank do not include collateral acquired in connection with the April 1994 debt restructuring.

(8) Internal public sector credits owed by other public sector entities. These amounts are consolidated into the consolidated gross public sector debt amounts above.

(9) Taxes receivable and demand deposits.

(10) Investments in public securities and short-term investments in public enterprises.

(11) Demand deposits.

(12) External credit available.

(13) Net public sector debt is consolidated gross public sector debt less aggregate credits of the federal Government and the Central Bank, State and local governments and public sector enterprises (excluding internal public sector credits that have been excluded from the calculation of consolidated gross public sector debt).

Source: Central Bank

Federal Domestic Securities Debt

Federal domestic (internal) debt is primarily in the form of bills and notes issued by the National Treasury or the Central Bank with an average maturity of about 19 months as of March 31, 1998. The Collor Plan required the lengthening of the average term of federal Government securities in circulation, while fostering a substantial reduction in the corresponding debt service burden. The following table shows the outstanding consolidated federal internal debt in the form of government bills and notes for the periods indicated.

Table No. 33

Consolidated Federal Internal Securities Debt(1)

	National Treasury Liabilities	Central Bank Liabilities	Total	Real Change For Period(2)
	(in millions of dollars)			
1994	41,761	31,268	73,029	19.7
1995	60,812	50,741	111,553	52.8
1996	89,577	79,955	169,531	48.7
1997	170,433	58,436	228,869	35.4
1998	181,311	86,629	267,940	17.1

(1) Securities issued by the federal Government to finance its current deficits and by the Central Bank for its open market operations. Consolidated to exclude debts between public sector entities. Data are for end of period. This table does not include liabilities related to the FCVS program. See "—Housing Compensation Fund for Salary Fluctuation (*Fundo de Compensação de Variações Salariais*)".

(2) Deflated by GPI-DS centered at the end of the month.

Source: Central Bank

The aggregate amount of the federal domestic securities debt held outside the Central Bank rose from $73.0 billion on December 31, 1994 to $267.9 billion on December 31, 1998, representing real growth of 165.2% in the aggregate amount of federal marketable securities and an increase from 13.4% of GDP to 34.5% of GDP. At March 31, 1999, the aggregate amount of federal domestic securities debt was $365.6 billion, or 37.5% of GDP.

To reduce the cost of servicing its domestic debt, the Government has been replacing its very short-term *Bônus do Banco Central* (issued by the Central Bank) with longer-term *Notas do Tesouro Nacional* (issued by the National Treasury), some of which are indexed to foreign currencies. Because the foreign currency-indexed bonds were sold at attractive interest rates (by international standards), they generated a substantial inflow of foreign capital until the Central Bank imposed new restrictions on foreign investment in August 1993. See "Balance of Payments and Foreign Trade—Foreign Investment".

Following the implementation of the *Plano Real* in July 1994, the level of inflation was sharply reduced and the financial markets began to accept fixed-rate federal Government paper with longer maturities. At March 31, 1998, such paper represented 51.0% of the total internal treasury instruments in circulation.

In September 1993, the National Treasury issued *Notas do Tesouro Nacional*, series L, securities having terms comparable with those of certain external debt of the Central Bank. On April 15, 1994, in connection with the Brady Plan exchange, the National Treasury redeemed those securities, reducing its domestic debt by 30.2% (approximately $27.3 billion) in real terms. See "—Debt Crisis and Restructuring".

Domestic Privatization Currencies

In addition to federal domestic securities debt in the form of bills and notes issued by the National Treasury or the Central Bank, the federal Government from time to time has issued securities that may be redeemed at face value in connection with the privatization of Government assets ("Privatization Currencies"). Privatization Currencies include, among others, Siderbrás debentures, Eletrobrás securitized credits and various credits extended to the agricultural sector. The aggregate amount of Privatization Currencies outstanding and not yet utilized for privatization purchases as of December 31, 1996 was R$12.0 billion. In addition, the FCVS securities proposed to be issued under Provisional Measure No. 1,520 will be eligible for use as a domestic privatization currency. See "—Housing Compensation Fund for Salary Fluctuation (*Fundo de Compensação de Variações Salariais*)".

Housing Compensation Fund for Salary Fluctuation *(Fundo de Compensação de Variações Salariais)*

Beginning in 1967, the Brazilian Government introduced a series of measures designed to provide subsidies to homeowners to address the effects of high inflation on mortgage rates. These subsidies were implemented in the form of the so-called *Fundo de Compensação de Variações Salariais* ("FCVS"), which was used to provide mortgage lenders in Brazil with a credit in an amount equal to the difference between the lender's actual cost of funds and the amounts that the mortgagor/borrower was legally obligated to pay under the terms of his mortgage. Under the FCVS program, the mortgagor/borrower was absolved of the responsibility to pay the amount guaranteed by the Government, and the lending institution recorded as an asset the amount of the FCVS subsidy receivable. The FCVS program has not covered any mortgages entered into after March 1990. The aggregate amount of the FCVS subsidy constitutes a liability of the Government; the FCVS subsidy is not accounted for as borrowed money and, therefore, is not reflected in the amount of the Republic's outstanding domestic public indebtedness. Although the macroeconomic effects of the FCVS subsidies (among others, the expansion of credit in the housing market and the continued growth of the housing sector) were largely absorbed by the Brazilian economy during the periods of high inflation during which the FCVS subsidy accumulated, a number of Brazilian financial institutions now hold large, illiquid stocks of FCVS assets (which, in turn, represent a liability of the Government on account of the subsidy).

In furtherance of the *Plano Real's* goals of restructuring the monetary and fiscal policies of the Government to ensure long-term economic stability and growth, the Government announced, in September 1996, a plan to issue securities in exchange for the accumulated liability attributable to the FCVS subsidy. This measure is intended to provide financial institutions holding FCVS assets with an opportunity to exchange such assets for newly issued, liquid, government securities.

The liability of the Government for the FCVS subsidy falls into two categories: (i) FCVS liabilities that relate to mortgages on which no further contractual payments are outstanding and which, therefore, are determinate as to principal amount ("determinate FCVS liabilities"); and (ii) potential FCVS liabilities that relate to mortgages on which additional contractual payments are due and under which additional FCVS liabilities may continue to accrue ("potential FCVS liabilities"). As of March 31, 1998, the Government had estimated that the aggregate amount of determinate FCVS liabilities would not exceed R$33.6 billion (of which R$19.4 billion is claimed as due and payable by the financial institutions receiving such credits and R$14.2 billion is claimed as payable but not yet due). The amount of the additional potential FCVS liabilities on outstanding mortgages is the subject of a Government audit and cannot be reliably estimated before such audit is substantially complete; however, the Government believes that if the new measures are effectively implemented, the amount of potential FCVS liabilities can be significantly reduced from the maximum of approximately R$34 billion that has been suggested in preliminary, unofficial estimates. Under the original FCVS program, the amounts payable thereunder accrued interest at an average rate of approximately TR+9.5% per annum. The Government plans to implement measures which are designed to reduce its FCVS liabilities generally by instituting auditing and verification procedures to ensure compliance with FCVS program requirements. In addition, the Government's proposal includes steps intended to reduce significantly its exposure for potential FCVS liabilities by offering incentives to homeowners to prepay FCVS loans, and by reducing the rate of interest payable on FCVS obligations.

The Government's FCVS initiative, as set forth in Provisional Measure No. 1,520 of September 24, 1996, provides that all properly audited FCVS claims can be exchanged for one of two new 30-year Government debt securities denominated in *reais*, one paying interest at a rate of TR+3.12% per annum and exchangeable for FCVS credits funded by housing finance institutions with resources made available through another Government program, the *Fundo de Garantia do Tempo de Serviço* ("FGTS"), and the second paying interest at a rate of TR+6.17% per annum and exchangeable for FCVS credits funded by financial institutions with savings deposits. The interest rates on the two new types of securities reflect the interest rates payable by financial institutions on FGTS funds and on savings deposits, respectively. The average rate of interest on such new securities would be approximately TR+5.1%, representing a significant reduction from the average rate of interest applicable to the existing FCVS liabilities. The new securities provide for an eight-year grace period on interest payments and a twelve-year grace period on payments of principal. The securities will be usable as domestic Privatization Currencies for purchases in privatization transactions. Because the amount of the new FCVS securities ultimately issued willl depend in part on the results of the Government's auditing process and on concluding satisfactory exchange agreements with the current holders of FCVS credits, it is not currently possible to predict the fiscal impact of the issuance of such new securities over the next few years. Although the issuance of securities in exchange for FCVS liabilities could, over time, require the recognition of domestic public sector debt, the Government believes that effective implementation of the auditing and verification procedures required by the new measure should result in a reduction in the aggregate amount of FCVS liabilities eligible for exchange for new securities.

External Debt

On December 31, 1998, Brazilian public sector medium- and long-term foreign debt was approximately $103.2 billion. This debt was incurred in large part as financing for Brazil's policy of growth through import substitution, which characterized the period from the 1950s through 1982. The bulk of the proceeds of this debt is used to finance large infrastructure projects and to strengthen the capital goods industry. At December 31, 1998, approximately $12.5 billion of this debt was owed to commercial banks, $13.2 billion to foreign governments, $21.6 billion to international financial institutions, $49.6 billion to bondholders and $6.3 billion to suppliers and other creditors. Most of the commercial bank debt was denominated in U.S. dollars and bore interest at floating rates. The Brady Plan-type debt restructuring of April 1994 substantially altered Brazil's external debt profile. Following that restructuring, the maturity profile of Brazil's public-sector external debt was substantially lengthened, from an average of 6.9 years at December 31, 1993 to an average of 8.8 years at December 31, 1996. The average maturity of Brazil's public-sector external debt has declined in recent years, reaching 7.7 years at December 31, 1997 and 6.9 years at December 31, 1998. In addition, prior to 1994, a very small percentage of Brazil's external indebtedness was represented by bonds; however, this percentage has increased significantly as a result of the April 1994 restructuring. While the interest arrearages were capitalized, the restructuring reduced previously outstanding principal obligations by about $4 billion. See "—Debt Crisis and Restructuring".

International capital market issues by the Republic since the April 1994 restructuring include the ¥80 billion 6% Notes Due 1997 in June 1995, DM 1 billion 9% Notes Due 1998 in July 1995, ¥30 billion 5.5% Notes Due 2001 in March 1996, Esc 12 billion LISBOR plus 240 basis points Due 1999 in May 1996, £100 million 9.75% Notes Due 1999 in June 1996, U.S.$750 million 8.875% Notes Due 2001 in November 1996, DM 1 billion 8% Bearer Bonds 1997/2007 in February 1997, FF 1 billion, NLG 400 million and ATS 2 billion 6.625% Parallel Bonds Due 2002 in May 1997, $3 billion 10⅛% U.S. Dollar-Denominated Unsecured Global Bonds Due 2027 (of which approximately $2.25 billion in aggregate principal amount was issued in exchange for certain outstanding bonds of Brazil issued in connection with

Brazil's April 1994 Brady Plan-type debt restructuring (see "—Debt Crisis and Restructuring—1992 Financing Plan")) in June 1997, ITL 750 billion 11% Bonds Due 2017 in two tranches in June and July 1997, £150 million 10% Bonds Due 2007 in July 1997, Euro 500 million 8.625% Bonds Due 2003 in March 1998, $500 million 10⅛% U.S. Dollar-Denominated Unsecured Global Bonds Due 2027 in March 1998, $1.25 billion 9⅜% Global Bonds Due 2008 in April 1998, DM 750 million Step-Down Bearer Bonds 1998/2008 in April 1998, $3 billion 11 5/8% U.S. Dollar-Denominated Global Bonds Due 2004 (of which $1 billion in aggregate principal amount was issued in exchange for approximately $993.1 million aggregate outstanding principal amount of El Bonds and approximately $200.4 million aggregate outstanding principal amount of IDU Bonds (see "—Debt Crisis and Restructuring—1992 Financing Plan)) and Euro 800 million 9.50% Notes due 2002.

The following table sets forth details of Brazil's public sector external debt by type of borrower at the end of the periods indicated.

Table No. 34

Public Sector External Debt by Type of Borrower(1)

	As of December 31,				
	1994	1995	1996	1997	1998
	(in millions of dollars, except percentages)				
Central Government	$75,701	$76,032	$74,009	$65,989	$ 66,775
Public Entities(2)	18,825	18,597	18,538	19,681	36,439
Guaranteed	11,838	11,872	10,211	10,111	19,771
Non-Guaranteed	6,987	6,725	8,327	9,570	16,668
Total(3)	$94,526	$94,629	$92,547	$85,670	$103,214
External Debt/GDP (%)	16.8%	13.2%	12.4%	10.7%	13.3%

(1) Debt with an original maturity of one year or more.

(2) Includes indebtedness of the Central Bank, public enterprises, mixed-ownership enterprises, semi-autonomous entities, States and municipalities.

(3) Private sector external debt (*i.e.*, debt with an original maturity of one year or more) totalled $25.1 billion in 1994, $34.7 billion in 1995, $51.5 billion in 1996, $82.1 billion in 1997 and $118.8 billion in 1998.

Source: Central Bank

The following table sets forth Brazil's public sector external debt by type of creditor at the end of the periods indicated.

Table No. 35

Public Sector External Debt by Type of Creditor(1)

	As of December 31,				
	1994	1995	1996	1997	1998
	(in millions of dollars)				
Commercial Banks	$ 8,771	$ 8,919	$ 9,869	$11,136	$ 12,500
Foreign Governments	19,495	18,993	15,592	13,226	13,233
Multilateral Organizations	10,098	10,039	10,015	10,436	21,622
Bondholders	52,858	53,711	54,526	49,069	49,566
Suppliers	630	491	397	430	700
Other	2,674	2,476	2,148	1,373	5,593
Total	$94,526	$94,629	$92,547	$85,670	$103,214

(1) Debt with an original maturity of one year or more. Includes indebtedness of the Central Bank, public enterprises, mixed-ownership enterprises, semi-autonomous entities, States and municipalities. Private sector external debt (*i.e.*, debt with an original maturity of one year or more) totalled $25.1 billion in 1994, $34.7 billion in 1995, $51.5 billion in 1996, $82.1 billion in 1997 and $118.8 billion in 1998.

Source: Central Bank

The following table sets forth Brazil's public sector external debt by currency at the end of the periods indicated.

Table No. 36

Public Sector External Debt by Type of Currency(1)

	As of December 31, 1995		As of December 31, 1996		As of December 31, 1997		As of December 31, 1998	
	(in millions)	(%)	(in millions)	(%)	(in millions)	(%)	(in millions)	(%)
U.S. Dollars	$64,936	68.6%	$64,360	69.6%	$57,916	67.6%	$ 66,965	64.9%
Japanese Yen	6,799	7.2	5,583	6.0	4,731	5.5	5,261	5.1
Due to World Bank(2)	6,037	6.4	5,876	6.3	5,552	6.5	6,224	6.0
Deutsche Marks	6,161	6.5	6,048	6.5	5,533	6.5	5,750	5.6
French Francs	4,570	4.8	3,665	4.0	3,003	3.5	2,751	2.7
Due to IDB(2)	3,853	4.1	4,066	4.4	4,839	5.6	6,425	6.2
Pounds Sterling	1,194	1.2	1,509	1.6	1,533	1.8	1,365	1.3
Swiss Francs	464	0.5	494	0.5	558	0.6	521	0.5
Canadian Dollars	240	0.3	195	0.2	178	0.2	154	0.1
Special Drawing Rights	142	0.2	68	0.1	32	0.0	4,795	4.6
European Currency Units	—	—	—	—	—	—	931	0.9
Others	233	0.2	683	0.7	1,795	2.1	2,072	2.0
Total	$94,629	100.0%	$92,547	100.0%	$85,670	100.0%	$103,214	100.0%

(1) Debt with an original maturity of one year or more. Includes indebtedness of the Central Bank, public enterprises, mixed-ownership enterprises, semi-autonomous entities, States and municipalities. Private sector external debt (*i.e.*, debt with an original maturity of one year or more) totalled $34.7 billion in 1995, $51.5 billion in 1996, $82.1 billion in 1997 and $118.8 billion in 1998.

(2) Consists primarily of Dollars, Yen, Swiss Francs and Deutsche Marks.

Source: Central Bank

The following table sets forth the amortization schedule of Brazil's public sector external debt by creditor.

Table No. 37

Public Sector External Debt Amortization Schedule by Creditor(1)

	Outstanding as of December 31, 1998	1999	2000	2001	2002	2003	2004	2005	2006	2007 and thereafter
				(in millions of dollars)						
Multilateral Organizations	$ 21,622	$ 5,972	$ 2,134	$1,449	$1,679	$1,580	$1,060	$ 749	$ 547	$ 3,455
Commercial Banks	12,500	2,594	901	2,261	1,021	541	703	1,276	430	2,678
Foreign Governments	13,233	1,847	1,332	1,308	1,314	1,418	1,540	1,691	1,862	765
Bondholders	49,566	2,254	2,139	2,208	1,751	2,040	3,278	3,518	2,844	29,533
Suppliers	700	2,174	2,210	263	222	87	73	33	14	501
Other	5,593	248	160	164	142	112	55	23	16	29
Total	$103,214	$15,089	$11,876	$7,653	$6,129	$5,778	$6,709	$7,290	$5,713	$36,961

(1) Debt with an original maturity of one year or more. Amortization figures in this table include only scheduled payments on outstanding debt as of December 31, 1998. Includes indebtedness of the Central Bank, public enterprises, mixed ownership enterprises, semi-autonomous entities, States and municipalities.

Source: Central Bank

On November 13, 1998, the IMF announced a $41.8 billion support package for Brazil, approximately $18.3 billion of which is to be provided by the IMF, $4.5 billion by each of the World Bank and the Inter-American Development Bank and $14.5 billion by 20 countries through a credit facility coordinated by the Bank for International Settlements and the Ministry of Finance of Japan. Brazil has received two sets of disbursements under that support package, totalling approximately $19.1 billion, in December 1998 and April 1999. On June 18, 1999, the Government repaid approximately 30% of the initial disbursement by the Bank for International Settlements and the Ministry of Finance of Japan, together with $221.8 million in interest. The remaining 70% was rolled over for another six months. Further disbursements under the support program are subject to the fulfillment of certain conditions. See "Introduction" and "The Brazilian Economy—*Plano Real* and Current Economic Policy".

On June 29, 1999, the Federal Senate approved an increase to $20 billion (or its equivalent in another currency) in the aggregate principal amount of bonds that Brazil is permitted to issue under its Program for the Issuance and Sale of National Treasury Bonds Abroad. The proceeds of any bonds issued under that program are to be used to refinance internal indebtedness of Brazil at a lower cost and for a longer term. The previous limit on Brazil's borrowing authority under the program was $10 billion (or its equivalent in another currency).

Debt Crisis and Restructuring

With the inception of the debt crisis in 1982, voluntary lending to Brazil by commercial banks ceased. With its foreign reserves in decline, Brazil struggled to make debt service payments by achieving substantial trade surpluses. Emergency lending by commercial banks and multilateral organizations in 1983 and 1984, together with a rescheduling of outstanding commercial bank debt, helped to stem the loss of reserves. In 1983, the IMF undertook to provide Brazil with 4.2 billion SDR (approximately $4.6 billion, as of December 31, 1982) over a three-year period, and commercial bank creditors agreed to reschedule $4.5 billion in principal payments and provide $4.4 billion in new money. Agreement was also reached with the country's foreign governmental (Paris Club) creditors that year, resulting in the restructuring of 95% of Brazil's principal and interest obligations falling due during the period from August 1, 1983 through December 31, 1984, as well as arrearages relating to the period from January 1, 1983 through July 31, 1983 in the aggregate amount of approximately $3 billion. In 1984, commercial bank creditors agreed to an additional rollover of $5.2 billion in principal and a new money facility for $6.5 billion in additional funds. Brazil's subsequent inability to meet all of the lending conditions established by the IMF led to a succession of new letters of intent and periodic suspensions of IMF disbursements.

Brazil did not seek new money from commercial banks in a 1986 debt rescheduling covering approximately $16 billion of 1985 and 1986 medium- and long-term maturities and approximately $15 billion of short-term trade and interbank lines. A sharp drop in reserves in 1986 as a result of a large capital account deficit and a sizable current account shortfall led the Government to declare a moratorium on principal and interest payments to commercial banks in February 1987.

1988 Financing Plan. In September 1988, Brazil's bank creditors agreed, among other things, to reschedule approximately $61 billion over a 20-year period pursuant to a Multi-Year Deposit Facility Agreement ("MYDFA") and to provide an additional $5.2 billion in new money pursuant to a Parallel Financing Agreement (a syndicated term loan), a Commercial Bank Cofinancing Agreement (a parallel cofinancing with certain World Bank project and sector loans), a New Money Trade Deposit Facility Agreement (to be used for medium-term trade finance starting one year after original disbursement) and New Money Bonds. Approximately $1.0 billion of Brazil Investment Bonds were also issued as part of this package, and approximately $15 billion of short-term lines were extended. The deal was accompanied by an IMF standby arrangement of $1.44 billion agreed in August 1988. The IMF suspended disbursements in 1989, however, because of the Government's inability to meet public-sector deficit targets. As a result, the third tranche ($600 million) of the $5.2 billion new money package was not disbursed. With reserves once again under pressure, the Government imposed new limitations on interest payments to holders of external commercial bank debt in July 1989.

Brazil initiated formal negotiations with commercial bank creditors in August 1990. As of January 1991, the Government permitted the full payment of external debts owed by private sector and financial institution borrowers and the servicing of 30.0% of interest payments due and payable by public sector obligors. Following the promulgation of Resolution No. 1,812 dated April 1, 1991 of the National Monetary Council of Brazil, the treatment previously accorded to private sector debt was extended to the external debt obligations of Petrobrás and CVRD and their subsidiaries. In April 1991, Brazil and the Bank Advisory Committee ("BAC"), consisting of twenty of Brazil's largest commercial bank creditors, reached agreement on the treatment of approximately $9.1 billion in interest arrears accrued on Brazil's external commercial bank debt through December 31, 1990. Under the agreement, the commercial banks received $2 billion of that amount in 1991, and the remainder of such past due interest was exchanged for approximately $7.1 billion aggregate principal amount of IDU Bonds on November 20, 1992 and March 18, 1993.

1992 Arrangements with IMF and Paris Club. In January 1992, Brazil reached agreement with the IMF on a standby facility of 1.5 billion SDR (approximately $2 billion). Of this amount, 75.0% was to have entered the country in the form of new money, while the remaining 25.0% was to have been used to finance the acquisition of collateral for the proposed restructuring of Brazil's medium- and long-term public sector indebtedness described below. The standby arrangement was subsequently suspended, however, because of Brazil's inability to meet agreed performance criteria targets, leaving 1.37 billion SDR undrawn as of the August 31, 1993 facility expiration date.

On February 26, 1992, Brazil reached agreement with Paris Club creditors for the rescheduling of debt owed other governments and governmental agencies totalling $12.1 billion. The agreement required Brazil to make approximately $4.1 billion in debt service payments in 1992 and 1993 and provided for the rescheduling of approximately $11 billion over a fourteen-year period, with a grace period of three years. Although Brazil has completed bilateral agreements implementing the February 1992 accord with all countries, debt relief for some maturities was conditional on continued performance under the IMF standby facility, and Brazil continues to discuss the impact, if any, of this condition with some countries. See also "—Debt Record".

1992 Financing Plan. On July 9, 1992, Brazil and the BAC reached an agreement-in-principle on the restructuring of Brazil's medium- and long-term public sector indebtedness owed to commercial banks, as well as on a parallel arrangement for interest arrears accrued in respect of such indebtedness since January 1, 1991. Pursuant to that agreement, on April 15, 1994, Brazil issued approximately $43.1 billion principal amount of bonds to holders of certain medium- and long-term public sector debt ("Eligible Debt") of Brazil or guaranteed by Brazil owed to commercial banks and certain other private sector creditors in consideration for the tender by such holders of their Eligible Debt and interest arrears accrued in respect thereof since January 1, 1991 ("Eligible Interest"). The bonds were issued pursuant to exchange agreements implementing the República Federativa do Brasil 1992 Financing Plan (the "1992 Financing Plan"), which provided for the restructuring of approximately $41.6 billion of Eligible Debt and arrangements for approximately $5.5 billion of Eligible Interest. Brazil's Financing Plan was a "Brady Plan"-type restructuring, the term coined for debt restructuring based on the policy articulated by U.S. Treasury Secretary Nicholas Brady in a speech before the Third World Debt Conference in March 1989. The Brady Plan advocated restructurings which would, among other things, (i) exchange debt for freely transferable bonds, (ii) result in significant reductions in the level of debt and the rate of interest payable thereon, and (iii) collateralize some types of new bonds with the pledge of U.S. Treasury zero-coupon obligations.

Holders of Eligible Debt exchanged their Eligible Debt for the following types of bonds: (i) Par Bonds ("Par Bonds"), (ii) Discount Bonds ("Discount Bonds"), (iii) Front-Loaded Interest Reduction Bonds ("FLIRBs"), (iv) Front-Loaded Interest Reduction with Capitalization Bonds ("C-Bonds"), and (v) a combination of New Money Bonds ("New Money Bonds") and Debt Conversion Bonds ("Debt Conversion Bonds"). Eligible Interest was exchanged (after giving effect to certain interest rate adjustments and cash interest payments made by Brazil pursuant to the 1992 Financing Plan) for EI Bonds (the "EI Bonds"). The Par Bonds, Discount Bonds, FLIRBs, C-Bonds, New Money Bonds, Debt Conversion Bonds and EI

Bonds are referred to herein collectively as the "Brady Bonds". Subject to their respective terms, each of the Brady Bonds is eligible for use as currency in the Brazilian privatization program.

The agreements implementing the 1992 Financing Plan provide for the collateral securing the Par Bonds and Discount Bonds to be delivered in four installments, with the last such installment to be delivered in April 1996. On October 12, 1995, the Republic accelerated its delivery of collateral by delivering the final installment on that date. As a result, the 1992 Financing Plan has been fully implemented.

The 1992 Financing Plan produced a reduction of approximately $4 billion in the stock of Eligible Debt; the $11.2 billion of Eligible Debt tendered for Discount Bonds resulted in the issuance of $7.3 billion of such bonds. In addition, the Government estimates that the 1992 Financing Plan will generate another $4 billion in interest savings over the 30-year repayment period. After giving effect to the completion of the phased delivery of collateral in October 1995, Brazil had approximately $17.8 billion of its external debt in the form of Par Bonds and Discount Bonds. The total cost of collateral to the Republic was approximately $3.8 billion.

At the Republic's option, the Brady Bonds may be redeemed at par in whole or in part prior to their maturity. The EI Bonds and New Money Bonds also include a mandatory redemption provision under which the Republic is required to redeem the EI Bonds and New Money Bonds at par if the Republic prepays certain obligations.

On September 12, 1996 the Federal Senate passed Resolution No. 69, which authorizes the Republic to repurchase or exchange its outstanding external indebtedness in the secondary market either for cash or for new securities issued by the Republic, provided that such repurchase or exchange of indebtedness permits the Republic to reduce its outstanding external indebtedness, reduce its debt service, lengthen the term of the indebtedness or otherwise improve the external debt profile of the Republic. Pursuant to Resolution No. 69, the Republic completed an exchange offer on June 9, 1997 pursuant to which $3 billion aggregate principal amount of the Republic's 10⅛% U.S. Dollar-Denominated Unsecured Global Bonds Due 2027 (the "Global Bonds") was issued. Of this amount, approximately $502 million in aggregate principal amount of Global Bonds was issued in exchange for Par Bonds, approximately $1.6 billion in aggregate principal amount was issued in exchange for Discount Bonds, approximately $94 million in aggregate principal amount was issued in exchange for C-Bonds and approximately $756 million in aggregate principal amount was issued for cash. Following the completion of the exchange offer, the Republic cancelled approximately $717 million aggregate principal amount of Par Bonds, approximately $1.9 billion aggregate principal amount of Discount Bonds and approximately $112 million aggregate outstanding principal amount of C-Bonds acquired by the Republic in the exchange offer.

In April 1999, Brazil completed a second exchange offer, pursuant to which $1 billion aggregate principal amount of the Republic's 11 5/8% U.S. Dollar-Denominated Global Bonds Due 2004 (the "Global Bonds") was issued in exchange for approximately $993.1 million aggregate outstanding principal amount of EI Bonds and approximately $200.4 million aggregate outstanding principal amount of IDU Bonds. The Republic sold an additional $2 billion aggregate principal amount of Global Bonds for cash. The settlement for both offerings occurred on April 30, 1999.

Certain Brazilian banks undergoing intervention or nonjudicial liquidation are holders of Brady Bonds. Certain of such banks owe significant sums to the Central Bank, which sums may be liquidated in whole or in part by the transfer of Brady Bonds to the Central Bank. In December 1997, approximately $5.3 billion aggregate principal amount of Par Bonds that had been pledged to the Central Bank by Brazilian banks undergoing liquidation were cancelled, following the sale of such Par Bonds to the National Treasury in exchange for National Treasury Notes.

The following chart sets forth certain summary information with respect to each series of outstanding Brady Bonds outstanding on December 31, 1998.

Table No. 38

Debt Securities Created by Brady Plan

Bond Type	Annual Interest Rate	Principal Repayment	Total Principal Amount of Bonds outstanding on December 31, 1998 (in millions of dollars)	% of Total
Par Bonds	Fixed rates stepping up from 4% to 6% in year 6 and subsequent years	4/15/24	$ 4,221	11.75%
Discount Bonds	Six-month LIBOR + 13/16%	4/15/24	5,409	15.06
FLIRBs	Various fixed rates stepping up from 4% to 5% in year 6; thereafter six-month LIBOR + 13/16%	in 13 consecutive equal semi-annual installments beginning 4/15/03	1,738	4.84
C-Bonds	8.00%(1)	in 21 consecutive equal semi-annual installments beginning 4/15/04(2)	8,605	23.96
New Money Bonds	Six-month LIBOR + 7/8%	in 17 consecutive equal semi-annual installments beginning 4/15/01	2,239	6.23
Debt Conversion Bonds	Six-month LIBOR + 7/8%	in 17 consecutive equal semi-annual installments beginning 4/15/04	8,490	23.64
El Bonds	Six-month LIBOR + 13/16%	in 19 consecutive semi-annual installments beginning 4/15/97	5,213	14.52
Total			$35,915	100.00%

(1) A portion of the interest payable under C-Bonds during the first six years from the April 15, 1994 exchange date will be capitalized as principal.
(2) Principal to be repaid under the C-Bonds includes capitalized interest.
Source: National Treasury Secretariat and Central Bank

Debt Record

As part of the reorganization of the public sector, particularly as initiated during the Collor Administration, the Republic has begun the liquidation of certain public sector entities and proceeded to assume their debts, both current and past due. In such cases, the Republic first confirms the amount and authenticity of the debts and then honors those obligations through the issuance primarily of instruments eligible for use in the privatization program or, in some cases, National Treasury Notes. This process is also applied to certain obligations of the Republic arising from internal financing mechanisms in the housing and electricity sectors.

The Republic has defaulted on and rescheduled loans from commercial banks and official creditors. See "—Debt Crisis and Restructuring". Throughout the debt restructuring process from 1982 to 1994, the Republic continued to make principal and interest payments on its external bonded indebtedness in accordance with the terms of such indebtedness. Prior to 1994, a very small percentage of Brazil's external indebtedness was represented by bonds; however, this percentage has increased significantly as a result of the Brady Plan-type restructuring described above.

TABLES AND SUPPLEMENTARY INFORMATION

Table No. 39

External Direct Debt of the Federal Government

	Interest	Issue Date	Final Maturity	Currencies	Amount Issued	Principal Amount(1) Outstanding At December 31, 1998
			(in millions of dollars)			
Multilateral Organizations						
International Monetary Fund (IMF)	Floating	Various	Various	SDR	$1,184.96	$ 10.95
World Bank	Various	Various	Various	Various	7,411.14	3,286.74
Inter-American Development Bank (IDB)	Various	Various	Various	Various	2,345.17	1,432.52
Total (Multilateral Organizations)						$ 4,730.21
Foreign Governments						
Foreign Governmental Agencies Original Loans	Various	Various	Various	Various	$2,394.23	$ 1,143.00
Paris Club Phase III	Various	29-Jul-88	01-Oct-99	Various	2,835.13	552.00
Paris Club Phase IV	Various	26-Feb-92	31-Dec-06	Various	12,294.57	9,505.96
Total (Foreign Governments)						$11,200.96
Bonds						
Brazilian Investment Bond (BIB)	6.0%	31-Aug-89	15-Jul-13	US$	$1,056.00	$ 900.16
1992 Bond Exchange Agreement(2)	Floating	10-Sep-92	01-Jan-01	US$	7,127.79	3,506.88
1994 New Money Bond	Floating	15-Apr-94	15-Apr-09	US$	2,239.06	2,239.06
1994 Debt Conversion Bond	Floating	15-Apr-94	15-Apr-12	US$	8,489.93	8,489.93
1994 Par Bond	Various	15-Apr-94	15-Apr-24	US$	10,491.14	4,221.10
1994 Discount Bond	Floating	15-Apr-94	15-Apr-24	US$	7,288.29	5,409.07
1994 Front-Loaded Interest Reduction Bond (FLIRB)	Various	15-Apr-94	15-Apr-09	US$	1,737.71	1,737.71
1994 Front-Loaded Interest Reduction with Capitalization Bond ("C" Bond)	Various	15-Apr-94	15-Apr-14	US$	7,406.24	8,605.00
1994 Eligible Interest Bond (EI Bond)(3)	Floating	15-Apr-94	15-Apr-06	US$	5,444.81	5,213.43
1995 DM Eurobond	9.0%	20-Jul-95	20-Jul-98	DM		
1996 "Samurai" Bond	5.5%	19-Mar-96	22-Mar-01	Yen	266.08	266.08
1996 "Caravela" Bond	Floating	13-May-96	13-May-99	ESC	69.72	69.72
1996 Pound Sterling Eurobond	9.75%	05-Jun-96	11-Jun-99	GBP	165.94	165.94
1996 Global Bond	8.875%	30-Oct-96	05-Nov-01	US$	750.00	750.00
1997 "Global BR-27" Bond	10.125%	09-Jun-97	15-May-27	US$	3,000.00	3,000.00
1997 DM Eurobond	8%	26-Feb-97	26-Feb-07	DM	602.11	602.11
1997 FRF Fungible Bond	6.625%	21-May-97	21-May-02	FRF	177.65	177.65
1997 ATS Fungible Bond	6.625%	21-May-97	21-May-02	ATS	169.43	169.43
1997 NLG Fungible Bond	6.625%	21-May-97	21-May-02	NLG	211.60	211.60
1997 Eurolira Bond	11%	26-Jun-97	26-Jun-17	ITL	450.75	450.75
1997 Euro GDP Bond	10%	30-Jul-97	30-Jul-07	GBP	248.91	248.91
1997 "Global BR-27" Bond	10.125%	24-Mar-98	15-May-27	US$	500.00	500.00
1998 "Global BR-08" Bond	9.375%	07-Apr-98	07-Apr-08	US$	1,250.00	1,250.00
1998 Euro Bond	8.625%	03-Mar-98	03-Mar-03	Euro	580.00	580.00
1998 DM Bond	10.0%	23-Apr-98	23-Apr-08	DM	451.58	451.58
Total (Bonds)						$49,216.19
Commercial Banks						
Import Financing Credits with Guarantee of Foreign Governments	Various	Various	Various	Various	913.00	353.03
Import Financing Credits without Guarantee of Foreign Governments	Various	Various	Various	Various	900.84	694.29
Loans	Various	Various	Various	Various	501.87	432.88
Total (Commercial Banks)						$ 1,480.20
Other						
Import Financing Credits with Guarantee of Foreign Governments	Various	Various	Various	Various	53.06	1.22
Import Financing Credits without Guarantee of Foreign Governments	Various	Various	Various	Various	246.12	145.53
Total (Other)						$ 146.75
Total						$66,774.31

(1) Currencies other than U.S. dollars are translated into U.S. dollars by the exchange rate (selling) at December 31, 1998.
(2) The original principal amount under the Bond Exchange Agreement was U.S.$9.1 billion including $2.0 billion of down payment.
(3) Capitalized interest.
Source: Central Bank

Table No. 40

External Debt Guaranteed by the Federal Government

	Interest	Issue Date	Final Maturity	Currencies	Amount Disbursed	Principal Amount(1) Outstanding At December 31, 1998
			(in millions of dollars)			
I. To Public Entities						
Multilateral Organizations						
International Monetary Fund (IMF)	Floating	Various	Various	SDR	$4,784.00	$ 4,784.00
World Bank	Various	Various	Various	Various	5,620.45	2,790.92
Inter-American Development Bank	Various	Various	Various	Various	4,335.38	3,843.62
Bank for International Settlements (BIS) ...	Floating	12-Dec-98	18-Dec-00	US$	4,150,000	4,150,000
Total (Multilateral Organizations)						$15,568.54
Foreign Governments						
Foreign Governmental Agencies Original Loans	Various	Various	Various	Various	1,482.81	1,161.62
Bonds						
1988 New Money Bonds	Floating	29-Sep-88	15-Oct-99	US$	674.74	96.39
Commercial Banks						
1988 Multi-Year Deposit Facility Agreement (MYDFA) Deposited at Central Bank	Floating	29-Sep-88	15-Sep-07	Various	(2)	1,114.43
Import Financing Credits with Guarantee of Foreign Governments	Various	Various	Various	Various	765.29	348.74
Import Financing Credits without Guarantee of Foreign Governments.....	Various	Various	Various	Various	268.14	26.81
Loans....................................	Various	Various	Various	Various	647.26	647.27
Total (Commercial Banks).................						$ 2,137.25
Other						
Import Financing Credits with Guarantee of Foreign Governments	Various	Various	Various	Various	42.74	8.01
Import Financing Credits without Guarantee of Foreign Governments.....	Various	Various	Various	Various	283.41	80.84
Loans....................................	Various	Various	Various	Various	579.72	190.79
Total (Other)						$ 279.64
Total for Public Entities						$19,243.44
II. To Private Companies						
(Including Privatized Companies)	Various	Various	Various	Various	1,768.49	818.69
Total.....................................						$20,062.13

(1) Currencies other than U.S. dollars are translated into U.S. dollars by the exchange rate (selling) at December 31, 1998.

(2) Not available. Corresponds to 100% of principal amount due to private banks from January 1, 1987 to December 31, 1990, plus 95% of 1991 maturities, 90% of 1992 maturities and 85% of 1993 maturities, defined as "Affected Debt" in the MYDFA. On December 1990, Brazil excluded 1991-1993 maturities of private and financial public sector debt from the Affected Debt concept. Affected Debt was initially estimated at $61 billion.

Source: Central Bank

Table No. 41

Internal Securities Debt of the Republic
Outstanding on April 30, 1998

Name	Index(1)	Interest Rate	Issuance Date	Final Maturity	Outstanding Amount(3) (millions of dollars)
National Treasury Letters (NTL) ..	—	— (2)	Various	Various	$ 87,583
A Series........................	US$	5.25% (Apr 98) 5.5% (Apr 98-Apr 99) 5.75% (Apr 99-Apr 2000) 6.0% (Apr 2000-Apr 2024)	Dec 97	Various (Oct 98-Apr 2024)	5,405
B Series	IGPM	6.0%	Oct 93	Oct 99	2,602
D Series	US$	6.0%	Various (Sept 93-Apr 98)	Various (May 98-Apr 2003)	19,572
P Series........................	TR	6.0%	Various (Jul 93-Mar 98)	Various (Jul 2008-Mar 2013)	12,076
L Series........................	US$	5.0%	Aug 97	Aug 99	1,804
R2 Series	US$	12.0%	Feb 94	Feb 2004	7
F Series........................	TR	5.0%	Jul 94	Sept 98	420
M Series	US$	Libor + 7⁄8%	Various (Apr 94-Sept 94)	Various (Apr 2009-Sept 2009)	303
T Series........................	TJLP	5.0%	Various (Apr 96-Sept 96)	Various (May 98-Jan 99)	956
I Series	US$	—	Various (Apr 94-Apr 98)	Various (Mar 98-Mar 2009)	316
J Series	Overnight	Mean Rate of NTL	May 96	Various (Nov 99-Nov 2002)	11,106
National Treasury Bonds........	US$/TR	6.0%	Various (Dec 89-Nov 90)	Various (Mar 99-Mar 2013)	53
Financial Treasury Letters (FTL) ..	Overnight	—	Various (Dec 97-Apr 98)	Various (May 98-Mar 99)	12,997
A Series........................	Overnight	0.245%(4)	Various (Dec 97-Jan 98)	Various (May 98-Jan 2013)	42,246
B Series	Overnight	—	Various (Dec 97-Mar 98)	Various (May 98-Jan 2006)	11,591
E Series........................	Overnight	—	(5)	Various (Aug 98-Mar 2006)	568
Total					$209,605

(1) Securities indexed to each indicated rate/index:
- Overnight = Central Bank's overnight rate
- IGPM = General Price Index (market based)
- US$ = U.S. dollar exchange rate
- TR = Index based on average daily rate of certificates of deposit issued by certain major Brazilian banks
- TJLP = Long-term interest rate index

(2) Zero-coupon securities issued at a discount from their face amount.
(3) Exchange rate (selling rate) at end of February 1997 (R$1.052 = US$1.00).
(4) Monthly interest rate.
(5) State-issued securities assumed by the National Treasury.
Source: National Treasury Secretariat

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FEDERATIVE REPUBLIC OF BRAZIL

12.75% U.S. Dollar-Denominated Global Bonds due 2020

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