BRAZIL – MEMORANDUM OF ECONOMIC POLICIES

I. BACKGROUND

1. Since the introduction of the *Real Plan* on March 1, 1994, the Brazilian economy has achieved a remarkable and sustained reduction of inflation, from an annual rate in excess of 2500 percent in 1993 to under 3 percent by September 1998—a rate that Brazil had not experienced for nearly half a century. Low inflation has been achieved without significant cost in economic activity or income loss. Real GDP grew at an average annual rate of 4.1 percent in 1994–97 and real GDP per capita at an annual rate of 2.7 percent. This economic performance—which contrasts sharply with the stagnation of real income and high inflation of the 1980s and early 1990s—allowed the maintenance of relatively low rates of unemployment through 1997, and a significant improvement in living standards of the Brazilian people, especially those in the lower income brackets.

2. Progress in macroeconomic and financial stability has been accompanied by substantial structural reforms, which have contributed to the modernization of the economy and to productivity growth. These reforms have included the continued opening of the economy through the liberalization of trade and capital flows, perhaps the largest privatization program in history, demonopolization and deregulation of key sectors of the economy, and a fundamental strengthening of the banking system (including the state banks). In such a context, it is not surprising that investment has risen from under 15½ percent of GDP in 1994 to an estimated 18½ percent of GDP in 1998, and that foreign direct investment (FDI) has risen from about US$2 billion to US$23 billion during the same period.

3. Despite the *Real Plan's* successes in macroeconomic stabilization, and structural reform, and despite the government's efforts to contain federal spending, modernize the tax system and strengthen its administration, and promote fiscal discipline at the state level, the finances of the nonfinancial public sector (NFPS) have remained a source of concern. It should be noted, however, that the public sector is defined very comprehensively in Brazil—more so than in many other countries—as it includes the federal administration, the social security, the central bank, the states and municipalities, and federal as well as state and local enterprises. This fact must be taken into account in any international comparative analysis of public sector statistics. It is clear by now, after four years of declining inflation, how different are the management and interpretation of the public sector finances in conditions of high and rising inflation, compared to conditions of low and stable inflation. Before the launching of the *Real*, *ex-ante* fiscal disequilibrium was largely transformed into *ex-post* equilibrium by rising inflation in a context of indexed revenues and only partially indexed nominal expenditures. With the advent of price stability, this adjustment mechanism, which masked to some extent the serious structural problems affecting the public sector, could no longer function. The weaknesses in the public finances have been manifested in a significant deterioration of the primary balance of the consolidated public sector which, in combination

with high interest rates, has contributed to the maintenance of substantial overall deficits of the public sector (in the range of 5–7 percent of GDP) in recent years, and to a steady climb in the ratio of the public debt to GDP.

4. The increasing dissaving of the public sector has necessitated a growing resort to external savings to finance the rise in domestic investment, leading to an increase in the current account deficit of the balance of payments from under ½ percent of GDP in 1994 to over 4 percent of GDP in 1997. Growing FDI has covered nearly 50 percent of this deficit, but total gross external debt has also increased, to about US$228 billion (over 28 percent of GDP) by mid-1998. It should be noted that since the early 1990s the Brazilian government has embarked on a major program of trade liberalization, with the virtual elimination of nontariff barriers and a sharp reduction of tariffs, and in a program of regional integration within MERCOSUL. This process has contributed to a significant increase in imports, especially of capital and intermediate goods, which has led to a sizeable increase in productivity but also to a temporarily high deficit in the merchandise trade balance and nonfactor services.

5. With the dramatic worsening of the international financial environment and the spread to other emerging markets of the Asian crisis in the last quarter of 1997, the *real* came under significant pressure. The central bank responded promptly by doubling its basic lending rate to 43½ percent, and the government enacted a package of revenue-raising measures and expenditure cuts equivalent to about 2½ percent of GDP. This timely and decisive tightening of policies succeeded in rebuilding confidence and allowing a gradual return of interest rates to pre-crisis levels. The high level of interest rates through the first months of 1998 and the emergency fiscal measures dampened, however, domestic demand—particularly for consumer durables—and restrained economic growth in 1998. The slowdown in economic activity contributed to a further decline in inflation, but also increased the unemployment rate from about 6 percent in 1997 to 7½ percent in September 1998. Some of this increase also reflects structural trends in the labor market, in particular the rationalization and modernization of production processes in industry and services.

6. The capital account came under serious pressure again in August 1998, in the wake of the crisis in Russia. The government's initial response was to adopt a number of administrative and tax measures to relax existing controls on capital inflows. It then tightened the stance of fiscal policy by enacting cuts in federal budgetary expenditures equivalent to 1.5 percent of fourth quarter GDP, a further cut equivalent to 0.3 percent of fourth quarter GDP in authorized investment expenditures of federal enterprises, a reduction in the disbursement of loans of federal banks to states and municipalities, the adoption of a binding target for the primary surplus of the federal government, and the creation of a high level interministerial committee responsible, inter alia, for ensuring the achievement of this target. This fiscal tightening was complemented by successive increases in the central bank lending rates and in the overnight interest rate, which reached 42½ percent in late October. These measures did moderate the rate of outflow of reserves, but did not succeed in halting it altogether. International reserves, which amounted to US$70.2 billion at end-July, declined to US$45.8 billion by end-September, and to around US$42.6 billion at end of October.

Although the rate of reserve loss moderated substantially in October, it became clear that a speeding-up of the pace of change in policy and reforms was needed. In a major public speech delivered 11 days prior to the elections, President Cardoso made clear to the country that a major fiscal adjustment and reform effort would represent a cornerstone of a second mandate for his government.

II. THE GOVERNMENT'S ECONOMIC PROGRAM

7. Economic policy in the years ahead will continue to aim at promoting sustainable growth of real per capita income, and improvement of the living standards of the Brazilian people, especially the lower income groups, in a context of low inflation and reduced vulnerability of the economy to external shocks. The achievement of these goals—particularly in the current and foreseeable international environment—will depend crucially on the ability to raise national savings, to finance the additional investments needed to increase productivity, competitiveness, and employment opportunities. The government's medium-term fiscal adjustment and reform program is aimed at promoting a steady increase in national savings, reducing the burden of the public debt, and facilitating a sustainable decline in interest rates.

8. The macroeconomic outlook for 1999 is inevitably conditioned by the current difficult international economic environment. Export growth is expected to be moderately strong, and imports are likely to decline, given the projected downturn of domestic demand. The resulting contribution of the external sector to growth should be considerable, but is unlikely to outweigh the fall in domestic demand, and real GDP may show a decline on average in 1999. From the fourth quarter of 1998 to the fourth quarter of 1999, however, real GDP should grow somewhat, since economic activity is expected to recover in the course of the year, and to accelerate to 3 percent and 4 percent in 2000 and 2001, respectively. The tight stance of monetary and fiscal policies, and the maintenance of the current exchange rate regime will contribute to keeping the rate of inflation to around 2 percent in 1999, a rate which compares well with those of Brazil's major trading partners. The external current account deficit is expected to decline from 4.2 percent of GDP in 1998 to around 3½ percent of GDP in 1999, and to be maintained around this level in subsequent years, despite the expected recovery in domestic demand. Reflecting the recent pattern, it is projected that more than half of the current account deficit will be financed by foreign direct investment in 1999.

9. To promote confidence and facilitate a sustained reduction in interest rates already during 1999, the government has announced a substantially front-loaded fiscal adjustment program. This program sets as a target for the primary balance of the consolidated public sector a surplus equivalent to 2.6 percent of GDP in 1999. This surplus is targeted to rise further to 2.8 percent of GDP in 2000 and to 3.0 percent in 2001. On the basis of conservative estimates regarding developments in interest rates, privatization revenues and the recognition of hitherto implicit public sector liabilities, these increasing primary surpluses are expected to arrest the growth of the net public debt in relation to GDP by 2000.

10. Within this framework, contributions to the fiscal adjustment effort are expected to be made by all levels of government, as emphasized by President Cardoso in recent pronouncements. Nevertheless, the bulk of the adjustment is planned at the federal level, which is targeted to achieve primary surpluses equivalent to 1.8 percent of GDP in 1999, 2.0 percent in 2000, and 2.3 percent in 2001. The magnitude of this effort is best appreciated by considering that, in the absence of any corrective action, the primary balance of the federal government would likely deteriorate from underlying equilibrium in 1998 to a deficit of 1.7 percent in 1999, and to even higher deficits in 2000 and 2001. In combination with the projected decline in interest rates, the improvement in the federal primary balance is expected to lead to a decline in the overall federal deficit from an estimated 5.6 percent of GDP in 1998 to 3.6 percent of GDP in 1999.

11. To achieve the targeted improvement, the federal government has announced a comprehensive set of expenditure-saving and revenue-raising measures, amounting in all to over 3 percent of GDP in 1999. Measures that have already been enacted by provisional decree or special regulations account for a substantial share of the revenue yield of the program. The recently approved administrative and social security reforms are expected to yield expenditure economies that, while small initially, will rise over time. Of greater importance for 1999, the government presented to Congress on November 9, 1998 a revised budget for 1999, including cuts in current and capital spending on goods and services, vis-à-vis the budget sent earlier, amounting to 20 percent of these expenditures and to nearly 1 percent of GDP. In distributing these cuts among different areas of spending, the government has strived to spare as much as possible spending on health, education and social protection.

12. The revenue-raising measures include: an increase in the rate of the tax on financial transactions (CPMF) from 0.2 percent to 0.3 percent, with a temporary surcharge of 0.08 percent for 1999; an increase in the rate of the tax on corporate turnover (COFINS), from 2 to 3 percent, one-third of which will be creditable against the corporate income tax; an increase of 9 percentage points in the contribution to the public sector pension plan by civil servants earning more than R$1,200 per month; the extension of this contribution to public sector pensioners (at the rate of 11 percent for those with pensions of R$1,200 per month or less and of 20 percent for the others); and a number of other measures aimed mainly at widening the bases of existing taxes and contributions, and eliminating distortions. These tax measures address the immediate fiscal adjustment problem, but the government will also introduce shortly a fundamental reform of the indirect tax system that will address the system's structural flaws (see paragraph 19). The government has emphasized that any modification of the proposed legislation by Congress which would impact adversely on the overall budget position, will need to be compensated by specific alternative revenue measures and/or further expenditure cuts.

13. The states and municipalities are expected to contribute to the fiscal adjustment effort with a shift in their consolidated primary balance from an estimated deficit equivalent to 0.4 percent of GDP in 1998 to a surplus of 0.4 percent of GDP in 1999, rising further to

0.5 percent of GDP in 2000 and 2001. To help ensure the achievement of these targets, the federal government will enforce firmly the commitments undertaken by the states in the context of their debt restructuring agreement with the federal government. The fiscal adjustment programs agreed with the states include specific targets for each state with respect to the primary balance, the revenue performance, the ratios of payroll and investment spending to revenues, and privatization and other structural reforms. The agreements also empower the federal government, if a state fails to service its restructured debt as scheduled, to withhold the revenue shared with that state and even to attach the latter's own revenues. In conjunction with the negotiation of these agreements, the government and the Senate, being mindful that unfettered access by the states to borrowed funds led to the escalation of state debt through the mid-1990s have moved to firmly limit the states' recourse to borrowing. Specifically, the Senate has forbidden new state bond issues, as well as new borrowing by states with a primary deficit; resolutions of the National Monetary Council have substantially reduced the limits for bank lending to the states and municipalities, as well as the limits on foreign borrowing by these entities. Also, the privatization or liquidation of most state banks, and the enforcement of strict prudential standards on the remaining ones, as well as the ongoing widespread privatization of state enterprises, have eliminated most avenues for deficit financing by the states.

14. The privatization of several profitable enterprises in recent years limits the contribution that this sector can make to the fiscal adjustment in the years ahead. Nevertheless, the government is targeting primary surpluses equivalent to 0.4 percent of GDP in 1999, 0.3 percent of GDP in 2000, and 0.2 percent in 2001, reflecting in particular efforts to increase productivity, contain costs and prioritize investments. The government also intends to ensure that federal enterprises maintain flexible pricing policies. In relation to PETROBRAS, which accounts for a large share of these enterprises' value added, the government has adopted a new policy to ensure an automatic pass through of changes in international petroleum prices to domestic prices.

15. The federal government plans to make fundamental changes to the management of its finances. A key element in its efforts will be the new Fiscal Responsibility Act, which the government will submit to Congress by December. The new law will set up a general framework to guide budgetary planning and execution. With a view to ensuring fiscal solvency, the law will, inter alia, establish prudential criteria for public indebtedness; provide strict rules for the control of public expenditures; establish standing rules to limit budget deficits, and prohibit any further refinancing by the federal government of state and municipal debt. In addition to these precepts, the law will include disciplinary mechanisms in the event that its targets and procedures are not observed.

16. The government views the recently passed constitutional amendment on social security reform as an important first step in this critical area. This legislation, together with the recently announced set of measures regarding social security contributions to the public pension system, will generate important savings over the next several years. They will not be sufficient, however, to ensure both the fairness and financial equilibrium of the system. To put social

security for both public and private sector workers on a sound footing and increase its fairness, while broadening the scope for individual choice, the government envisions a complementary set of new legislative initiatives, to be presented to Congress in the first quarter of 1999. The guiding principle of this complementary round will be the principle of actuarial balance. Notional individual accounts will be set up for participants of both the private system (RGPS) and the public system (RJU-federal), and the link between a worker's accumulated contributions and expected pension will be made much tighter.

17. The size of the RGPS will be limited by imposing a cap of R$1,200 per month on the salary base for the employee's contribution. The employer's share of the tax will continue to apply to that part of salaries that exceeds R$1,200, but this extra revenue will not form part of the employee's salary base for the purposes of determining the pension. There will also be a number of reforms to improve the finances of public sector pension plans other than the RJU-federal. A minimum plan size—5,000 contributors—will be established. Individual accounts will be obligatory, and a cap will be placed on the ratio of employer to employee contribution rates of 2:1, and a number of automatic triggers for increasing contribution rates in the event of financial imbalances will be established. Finally, a regulatory system will be put in place to help ensure compliance of public sector plans with the new legislation.

18. The passage of the administrative reform was one of the important achievements of the first administration of President Cardoso. To bring this reform effort to a successful completion, the government has already submitted to Congress various enabling laws and regulations, with the aim of ensuring that the reform begins to produce effects already in 1999. The main objective of the reform is to increase the efficiency and reduce the cost of public administration. The probationary period required of all newly recruited civil servants will be lengthened and civil servants will be liable for the first time to dismissal for inadequate performance, on the basis of periodic evaluations. The enabling legislation will also allow governments to enact the Administrative Reform's proposals for the elimination of over-staffing. These reforms will apply at all levels of general government, and will help governments meet the targets of the *Lei Camata*, which sets a cap on government payroll spending as percentage of revenues. The federal government is empowered to suspend discretionary transfers to those subnational governments that are not in compliance with the *Lei Camata's* target.

19. Brazil's current indirect tax system is inefficient and unduly complex; it includes cascading taxes which hamper Brazil's competitiveness; it superimposes different taxes levied by the various levels of government at different rates and with different definitions of the base, fostering wasteful tax wars among the states, and increasing the scope for tax avoidance and evasion. The government is, therefore, attaching great importance to presenting to Congress before the end of this year tax reform legislation that will address these weaknesses. The reform is expected to create a nationwide VAT, with a common base and rate structure, that is shared among the different levels of government and administered by the states. The new VAT will replace a number of existing taxes, thereby greatly simplifying tax administration and reducing distortions. Appropriate adjustments will need to be made in the system of

revenue sharing among different levels of government, to ensure that any losses or gains induced by the reform are compensated for. No major changes are being planned to the income taxes and other taxes collected by the federal government. The government intends to continue its efforts to improve tax administration and in particular, to introduce legislation to strengthen the Federal Tax Secretariat, by giving it increased autonomy, and by upgrading the training of tax officers, and rationalizing their salary structure to increase the incentives for good performance. It also will continue—in collaboration with other IFIs—its support to the efforts by state and municipal governments to strengthen their tax administration.

20. The social security system's financial problems have been aggravated by a high rate of evasion of the payroll tax. The social security administration plans to take steps to address this unsatisfactory situation. It will begin cross-checking its own accounts with information from the tax department on the incomes of the self-employed, whose evasion rate is particularly high. Measures will also be taken to upgrade processing systems, and to improve information on tax payments and returns. Finally, a system designed specially to monitor the compliance of the country's 10,000 largest taxpayers will be set up. This reform program could be expected to increase social security revenue progressively over time, although the projections of the yield of the adjustment effort in 1999 make no allowance for it.

21. The government recognizes there is considerable scope for rationalizing the operations of government, and for improving the budgetary process. The federal government is still carrying out certain functions that would be more appropriately assigned to the states. More generally, the government has begun to plan to introduce in the year 2000 a more rigorous system of program appraisal to evaluate programs on the basis of their success in achieving well-defined objectives at minimum cost. All budget line items will be grouped under one program or another and a thorough reappraisal of existing programs will be carried out to assess whether they are still in line with the government's priorities.

22. Well-targeted and efficient social expenditure programs play a vital role in the alleviation of poverty and in the development of human capital. Apart from the pension system, most social expenditure programs are in the domain of the states, but the federal government is responsible for financing a part of this expenditure, and has social expenditure programs of its own. The government intends to give priority to primary education and basic health core in the allocation of social expenditures, to promote the more efficient use and financing of health and education, particularly at the higher levels; and to better target social expenditures to the poor. To this end, the federal government will minimize budgets cuts on social expenditure programs that benefit the poor, while striving to improve their targeting and cost effectiveness. These efforts are expected to be supported by the World Bank and the IDB.

23. In the past few years the Brazilian Government has undertaken one of the most ambitious privatization programs in the world. It has involved both the federal and subnational governments; has encompassed industries as diverse as telecommunications, energy, ports, railways, mining, steel, urban transportation, and financial institutions, and has been successful

in attracting substantial participation by foreign investors. In 1999 the program will focus on the public utilities—which, in many countries, remain in the public domain. The companies to be privatized comprise most state-owned companies in the electrical sector—power generation and distribution—some of the remaining state banks, such as Sao Paulo's former state, now federal, Bank Banespa, the IRB Brazil Reinsurance S.A., and some water, gas, and sewerage public utilities. Competition in the recently privatized telecommunications sector will be fostered through concessions to the private sector. Concurrently, the government will continue its review of the regulatory framework for privatized public services and sectors.

24. The process of privatization and dismantling of public monopolies is contributing to the provision of better and more efficiently produced goods and services, and to the renovation and modernization of the country's capital stock. Deregulation of the economy and the increased participation of foreign capital has generated important price and technological externalities, raised productivity, improved resource allocation, modernized management practices, and connected Brazilian corporations with major global players, thereby improving the long-run prospects and efficiency of the economy.

25. The priority goal of monetary policy is continued low inflation. The current exchange rate regime is an essential means to this end. The central bank will continue to apply a flexible interest rate policy as appropriate to support the *real*, while safeguarding foreign exchange reserves. As the adjustment effort takes hold and confidence is rebuilt, interest rates will be allowed to decline. The central bank will continue to rely on the indirect policy instruments it has been using to guide short-term interest rates: specifically, it will influence bank liquidity as necessary through auctions of its securities, and interventions in the overnight market, and it will use its rediscount (TBC) and upper-tranche liquidity support (TBAN) rates as signaling devices to guide the formation of expectations about the general course of interest rates.

26. In the management of the domestic public debt, the treasury and the central bank will give priority to securing a progressive lengthening of the maturity of the debt to reduce gross refinancing requirements. The expected decline in interest rates, as risk premia on the Brazilian and domestic debt are reduced by the recovery of confidence, will provide an opportunity to begin increasing again the share of fixed rate securities in the debt at an acceptable cost. In this regard, the central bank plans to step up its recent issues of securities with sequential maturities at fixed and variable rates, increasing progressively the length of the fixed rate maturity, in line with market demand. It is also the authorities's intention to maintain within prudent limits the share of dollar-indexed public debt in the total debt, and to continue lengthening its maturity as market conditions permit.

27. Although the high interest rates of the past year have put a strain on some of the country's smaller banks, the banking system as a whole has weathered this period well. The share of nonperforming loans in total loans outstanding did rise from 6.9 percent as of December, 1997 to 8.3 percent in August 1998, but provisioning for bad loans reached 145 percent in that month. The acquisition in 1998 of three of the country's large- and medium-sized banks by large foreign banks is a positive aspect of the ongoing rationalization

of the industry, which has weeded out weaker institutions and put the rest on a sounder financial footing. Capital adequacy ratios among the top private domestic banks are on the order of 15 percent (tier 1 capital) or higher, which is well in excess of Basle recommendations.

28. The legislative and supervisory framework has been considerably reinforced since the inception of the *Real Plan*, and in the last two years in particular. The minimum capital adequacy ratio was increased from 8 percent (tier one) to 10 percent of risk-weighted assets as of December 31, 1997, and will be at 11 percent with effect from January 1, 1999. Since July 1997, banks have been required to make a capital charge against the counter-party credit risk of derivative operations that exceeds Basle norms. Bank credit risk analysis has also been facilitated by putting in place in the course of 1997 a Credit Risk Center, which allows the authorities to determine the sum of a borrower's indebtedness to domestic financial institutions. Bank supervision, which has been the object of assistance from the World Bank, has been considerably strengthened by the institution of comprehensive on-site inspections and audits, and measures have been enacted to ensure that if the operations of offshore affiliates are not subject to full supervision, the parent must make full provision against the assets of the affiliate. A law enacted in March 1997 stipulates that undercapitalized banks are to be recapitalized within six months of being notified by the central bank, and requires a related memorandum of understanding that is subject to monthly audits. In sum, considerable strides have been made in implementing the 25 basic principles of the Basle Committee on Banking Supervision, and the government believes that Brazil can be fully compliant by the year 2000.

29. The difficulties of the state banking system are now largely resolved. The number of state financial institutions will have been reduced from 35 to 11 once the restructuring process is concluded, and their share in the total deposits of the Brazilian financial system is to be reduced by two-thirds to about 7 percent of the total by end-1999. The government intends to subject the remaining banks to the same regulatory and supervisory scrutiny as the private banks. All of the measures described above will bolster confidence in the banking system by strengthening its safety net, which is based on a solid supervisory and regulatory framework, the lender-of-last resort function, efficient insolvency procedures, and protection for depositors. In this connection, the government plans to add a "stand-by" facility to the deposit insurance fund to improve its finances, and will take measures to speed up the resolution of failed banks, and to increase asset recovery rates.

30. The government is fully committed to maintaining the present exchange rate regime. The current policy of gradual devaluation of the *real*, in conjunction with the ongoing structural changes and the significant productivity gains of the Brazilian economy, will contribute to the strengthening of the export performance and to an efficient import substitution process, improving overtime the external sector accounts. While maintaining the current regime, the central bank will continue its policy of gradually widening the exchange rate band. Within this band, the management of the exchange rate will be aimed at rebuilding reserves and increasing the competitiveness of the economy.

31. The government intends to continue the policy of trade liberalization, which characterized the first mandate of President Cardoso. It will continue to promote the integration of the Brazilian economy with those of its MERCOSUL and other regional trading partners, and will also aim to increase trade with countries outside the region. Brazil will not impose trade restrictions which are inconsistent with the WTO commitments or, within the context of a program with the Fund, restrictions based on balance of payments reasons. Brazil has strengthened institutional capacity to deal with antidumping and other nontariff mechanisms in line with agreements reached within the context of the WTO. The recent adoption of stiffer measurement and quality standards, flat import fees, and the nonautomatic licensing for selected imports is not expected to have a relevant impact on import volumes. The government will continue to promote the competitiveness of Brazil's exports through steps aimed at leveling the playing field for Brazilian exporters, facilitating access to financing and to export credit insurance, in line with WTO regulations.

32. Brazil's external debt is not very high in relation to GDP (29 percent), and its average maturity is relatively long. The public sector component of the external debt accounts for no more than one-third of the total, and public sector short-term debt is less than US$6 billion. It is the government's intention to keep the increase of the public sector external debt within prudent limits, around US$10 billion in 1999. It is also the government's intention to promote a gradual further lengthening of the average maturity of the total external debt, as market conditions permit. There is also scope for improving the overall monitoring of external debt, and in particular for compiling and disseminating more timely information on composition by type of instrument and creditor. The government will take action to deal with these shortcomings in the information base, and in this connection, will seek assistance from the Fund or other relevant agencies.

33. Although the Brazilian labor market is not beset by severe rigidities, certain labor market regulations and policies can contribute to greater flexibility and to the increase of labor productivity and formal employment. In face of the recent increase in unemployment—which results both from structural and cyclical factors—the need to reform the labor legislation and to improve labor market policies has become more urgent.

34. The government has taken major steps in modernizing the labor legislation and improving labor market policies. The following measures have already been implemented: (i) adoption of a temporary lay-off system in order to reduce final separations; (ii) regulation of part-time and temporary contracts; (iii) flexibility of working hours in order to reduce overtime costs; (iv) extension of unemployment insurance benefits for long-term unemployed workers and (v) improvements in the training and retraining system. Besides these measures, the Administration has recently sent to Congress a proposal of constitutional reform which reduces the restrictions for union organization and creates incentives for direct collective bargaining between unions and employees. These measures and proposals are aimed to provide a more encompassing safety net for the unemployed, reduce job destruction, increase the proportion of formal labor contracts and promote labor productivity.

35. Brazil's statistical base is in many respects very well developed. There remain, however, some areas of weaknesses that the government intends to address in the near future. The national accounts, in particular, include data on the components of aggregate demand in current prices but those in constant prices are based on outdated weights. The official monthly labor market survey is for the moment restricted to the country's six largest metropolitan areas. The central government's accounts are produced on a monthly basis, but the federal character of Brazil's government and the diversity of the states makes such a standard unrealistic for general government as a whole. Monetary and financial statistics have generally good coverage, but improvements need to be made in the sectoral classification of assets. The coverage of external debt is good, but detailed statistics are available only with a lag. Brazil has recently received technical assistance from the Fund in money and banking statistics, and has been working with the Fund to improve the timeliness of the debt statistics. It will accelerate work on the national accounts, and as a part of this effort, intends to ask for further technical assistance from the Fund. As a measure of its commitment to improving Brazilian economic statistics, the government has decided to subscribe to the SDDS as soon as technically feasible and plans to ask for technical assistance from the Fund to advise on the status of the statistical system vis-à-vis the SDDS requirements.