1. The Government of Brazil has consulted the Fund under Article XIV, Section 4, of the Fund Agreement concerning the further retention of its transitional arrangements.

2. The Brazilian economic and financial situation continued to deteriorate in 1963 and the first quarter of 1964 despite efforts early in 1963 to limit credit expansion and to improve the budget. Despite a growth in real value of tax receipts, the 1963 budget deficit continued to increase in real terms due to the growing personnel costs and increasing subsidies to state agencies. During the full year bank credit to the private sector continued to expand at an undiminished rate though in the first half of 1963 there was a transitory reduction in its rate of growth; there were also increased losses to the Bank of Brazil on exchange operations. Currency issue rose at a record rate and by early 1964 price increases were exceeding 100 per cent per annum. Production was disappointing because of adverse weather and the effects of the inflation, and production per capita may have declined. The balance of payments showed a limited improvement primarily because of, first, an increase in the volume of coffee exports, and later, of an increase in coffee export prices, but a deficit continued and arrears mounted.

3. The Brazilian authorities believe that the inflation is causing serious economic damage and they are preparing an economic program designed to slow the rate of inflation. Particular emphasis is being placed on the need to reduce the budget deficit and eliminate subsidies. Some important steps in this direction have already been taken, including the virtual elimination of exchange subsidies and the submission to Congress of proposals for increased taxation. On the other hand, the Government has also granted some very substantial salary increases payable from the budget.

4. Measures to achieve external equilibrium are urgently needed and a strenuous effort should be made to reduce commercial arrears and to meet foreign obligations. To deal with the heavy burden of foreign debt, the authorities plan
to resume the approach to creditors to renegotiate schedules of payments. The Fund hopes that a mutually satisfactory debt arrangement can be agreed between all parties in the near future and that effective measures can be taken to avoid the recurrence of excessive debt service.

5. The Fund welcomes the recognition by the authorities of the damage caused by the inflation and urges that an effective program to bring an early end to the inflation be pursued. Of key importance are the reduction of the budget deficit to a level which can be financed from noninflationary sources, the adoption of an adequate wage policy designed to break the wage-price spiral, and of a credit policy designed to achieve stability of prices.

6. The Fund considers that the changes in the exchange system in March and May 1964 were important steps forward. The Fund welcomes the plan to reduce the advance import deposits and to eliminate the minor preferential rate for fuel oil and liquid gas. In the meantime, the Fund does not object to the continuation on a temporary basis of Brazil's multiple currency practices and restrictions.

7. In concluding the 1963 Article XIV consultations, the Fund has no other comments to make on the transitional arrangements maintained by Brazil.