BRAZIL -- 1961 Art. XIV Consultations and previous consultations not discussed by Board

BOX 1
File 8

ETRAI IRVING S. FRIEDMAN COUNTRY FILES

INTERNATIONAL MONETARY FUND

April 20, 1959

Mr. Friedman:

No comments.

JWG

J. W. Gunter

INTERNATIONAL MONETARY FUND

TO : Mr. Friedman April 17, 1959

FROM : A. S. Gerstein

Subject: 1958 Article XIV Consultations - Brazil

The Legal Department has no comments to make on the Report other than those which have been transmitted to Mr. Costanzo.

APR 15 1959

To: Members of the Committee on Article XIV Consultations

From: The Chairman

Attached for your review is the draft staff report on

Brazil, together with background material (Part II).*

I would appreciate receiving your comments by 5 P.M. (hour), Friday (day),

April 17, 1959 (date).

Mr. Anwar Ali Gunter
Mr. Del Canto Friedman
Mr. Ferras
Mr. Raj - Sankar

Mr. Gardner
Mr. Gerstein
Mr. Kroc ✓

as amended on page 4, Part I.

I suggest issuing a separate paper which would state that the Art. XIV consultations were also the consultations under the stand-by arrangement and that Brazil is not eligible to use the Fund's resources. 4-16-59

Discussed with Costanzo and others Apr. 16. Agreed not advisable to do separate paper at this time.
ISF

*Part II will be issued tomorrow.

To
Mr Friedman

Seen. Thanks. No comments.
J.J.Raj

APR 15 1959

To: Members of the Committee on Article XIV Consultations

From: The Chairman

Attached for your review is the draft staff report on Brazil, together with background material (Part II).* I would appreciate receiving your comments by 5 P.M. (hour), Friday (day), April 17, 1959 (date).

Mr. Anwar Ali
Mr. Del Canto
Mr. Ferras
Mr. Raj ✓

Mr. Gardner
Mr. Gerstein
Mr. Kroc

*Part II will be issued tomorrow.

APR 15 1959

To: Members of the Committee on Article XIV Consultations

From: The Chairman

Attached for your review is the draft staff report on Brazil, together with background material (Part II).* I would appreciate receiving your comments by 5 P.M. (hour), Friday (day), April 17, 1959 (date).

No comment

European Dept

Derek O'Connor

4/16

Mr. Anwar Ali
Mr. Del Canto
Mr. Ferras ✓
Mr. Raj

Mr. Gardner
Mr. Gerstein
Mr. Kroc

Brian

Could Charles take a quick look at this?

*Part II will be issued tomorrow.

Brazil concluded new bilateral trade and payments agreements during the year with East Germany, Rumania, and Yugoslavia. Current transactions under these agreements are to be settled in U.S. dollars, and there are provisions for Brazil to extend to export receipts and import payments through the accounts exchange treatment equal to that granted to exports and imports paid for in externally convertible currencies.

INTERNATIONAL MONETARY FUND

Brazil

1) prices up. – 35% in 1958 – 1959 –
2) increase in currency issue
3) rapid expansion in Banco do Brasil credit.
4) Fed. Govt deficits – sharp increase in expends.
5) ~~large~~ public sector deficit, part. railroads
6) coffee support financing
7) Bal/payts –
  a) exports down $170 m.
  b) imports down $70 million
  c) losses $200 m. in 1958 + repayments of $50m.
  d) 30% of earnings to pay debts + amortizations – $64 mil
8) ~~free~~ auction rate – at Cr$ 296. (85 to 296 – in 15 months
9) 1959 program
  a) budget deficit of Cr$ 12 billion – means economy in Cr$ 35 billion (20% cut,
  b) over-all credit expansion of Cr$ 55 billion, or 15-20% –
  35 bill to private sector or 18%
  c) coffee – surplus of 12 to 14 million bags

Irving S. Friedman

16 million exported – Cr$ 15 billion
+ 6 – 21 billion outlays

INTERNATIONAL MONETARY FUND

Monetary policy

1) no further substantial change

2) not realize profit at [illegible] & [illegible],
[illegible]: US$ 300 million aid –

3/ foreign debt: – restrict foreign suppliers' credit.
forecast deficits of $306 m. in 1959 and
$250 m. in 1960

Exchange System

① some simplification of export and
import rates:

② merging [illegible] + Hague Club.

(3) depreciation of structure

(4) more bilaterals

Irving S. Friedman

INTERNATIONAL MONETARY FUND

P39

The staff's report at the time indicated that a comprehensive ~~[illegible]~~ review of the exchange system was contemplated for ~~the~~ early 1959.

Irving S. Friedman

INTERNATIONAL NETARY FUND

Irving S. Friedman

p 32

Thus, the last year has seen
certain improvements in the exchange
system in that certain rates
have been merged and the
structure made ~~rea~~ more dependable.
However, the system still
remains highly complex ~~and~~ ~~[illegible] with~~ the technique
in clarity
only
while the continuing inflation
has made
~~bad~~ ~~Affect the~~
the structure even more unrealistic

INTERNATIONAL MONETARY FUND

Irving S. Friedman

Belgo-Egyptian: (Nov 1957)

1957 — 1959

Exports

4 categories

2 loans

[illegible]

3 categ

no loans

but free market

Import

auctions

General

Special

Penalized Imports

INTERNATIONAL MONETARY FUND

This is old Part I "restrictive system" section.

G. A. Costanzo

3. The restrictive system

a. The system in November 1957. When the staff held discussions with Brazil in November 1957 in connection with the 1957 Consultations, the exchange system, comprising fixed and fluctuating rates, included two export bonuses for each of four categories of export proceeds, and fixed surcharges and auction premiums for import payments. Although limited use was made of import licensing for certain commodities, such licenses were issued freely--either to holders of exchange certificates purchased at auction, or for preferential imports authorized within global quotas. All transactions in nontrade invisibles and most capital transactions took place at a fluctuating free market rate.

Exports were divided into four categories with two different bonuses for each category--one bonus for export proceeds in convertible currencies, ACL currencies[1] and Argentine clearing dollars, and a smaller bonus for proceeds in all other currencies. The bonuses were additional to the official buying rate of Cr$18.36 per U.S. dollar. Coffee exports (Category I) received an additional bonus varying with the price of coffee; and textile exports were given a bonus of Cr$36 per U.S. dollar. Incentives were given to a number of export commodities through a "symbolic purchase" scheme operated by the Bank of Brazil.[2] Effective export rates against convertible and ACL currencies, and Argentine clearing dollars ranged from Cr$37.06 for coffee exports (Category I) to Cr$67 for Category IV exports (the rate for textile exports was Cr$103).

---

[1] Sterling, deutsche mark, Netherlands guilders, Belgian francs, Italian lire, and French francs.

[2] According to this scheme the Foreign Trade Department of the Bank of Brazil purchased such commodities from producers at prices fixed by the Department and then exported the commodities. The Foreign Trade Department met the difference between the price paid to the producers and the local currency equivalent of the exchange surrendered to the Bank of Brazil at the established effective exchange rate by drawing on the exchange differential (agio) account.

In order to allocate exchange according to essentiality, payments for nonprivileged imports were effected by means of an exchange cover or an exchange certificate purchased at either a General Category auction or a Special Category auction. The General Category included imports of raw materials, equipment, and other production goods, and essential consumption goods in short supply in the domestic market; the Special Category consisted of other goods. At the end of November 1957 the premium in the General Category auction was about Cr$62 per U.S. dollar, and for the Special Category about Cr$205 per U.S. dollar, giving effective rates of about Cr$80.82 and Cr$223.82, respectively.

For privileged imports there was a range of effective rates--Cr$18.82 for newsprint; Cr$51.32 for wheat and specified government imports, and imports for the petroleum and printing industries; Cr$53.82 for imports of most petroleum products; and preferential rates resulting from specific auctions for imports of fertilizers, insecticides, and fruit. Apart from the above arrangements, special exchange rate treatment was extended to imports of component parts of motor vehicles for assembly in Brazil. Of the total expenditures in foreign exchange by Brazil for imports and related invisibles at this period, about 52 per cent was for payments effected at preferential rates of exchange, the remainder going through auction markets.

All transactions in invisibles not directly related to the movement of goods and most capital transactions took place in the free market where the average commercial bank selling rate at the end of November 1957 was Cr$92 per U.S. dollar. At that time, apart from the Hague Club arrangements, Brazil had bilateral payments and/or trade agreements with 15 countries, and also maintained bilateral relationship on a <u>de facto</u> basis with Denmark and Sweden. In particular, bilateral agreements were a significant feature of Brazil's trade with Latin American countries.

b. Developments since the last consultations. By adjustment of the bonuses and category composition in respect to export proceeds and through variations in the level of the surcharges imposed on payments for imports, an effective depreciation of the Brazilian exchange system occurred on several occasions during 1958 and early 1959. On June 10, 1958, the bonuses for exports in Categories III and IV were increased, but the effective rates for coffee and cocoa (Categories I and II, respectively) were left unchanged. The bonuses were henceforth applied uniformly to the proceeds of exports to all monetary areas, revoking the previous distinction between receipts in convertible, ACL currencies and Argentine clearing dollars, and other currencies. The previous Cr$36.64 bonus for Category III exports was increased to Cr$51.64, giving an effective rate of Cr$70 per U.S. dollar, and the composition of the category was also varied. The bonus for Category IV was set at Cr$73.64 (previously Cr$48.64) with an effective rate of Cr$92 per U.S. dollar. Subsequently, proceeds from the exports of precious and semiprecious stones and reading material published in Brazil were transferred from the Cr$92 rate to the fluctuating free market, which had formerly been limited to capital and invisible transactions. Apart from these changes, the special rate for textile exports was eliminated, and the "symbolic purchase" scheme which had given rise to a multiplicity of buying rates was abandoned. Also, the mining industry had been authorized on March 17, 1958 to retain abroad 30 per cent of its export proceeds to service registered loans used for payment of goods and services to develop the industry.

Concurrently with changes in the export bonuses, the import surcharge was increased from Cr$32.50 to Cr$40 in the case of certain preferential imports and official payments (i.e., the effective rate was depreciated from Cr$51.32 to Cr$58.82 per U.S. dollar); and other commodities formerly classified at the preferential Cr$51.32 rate were moved to a new rate of Cr$70 per U.S. dollar (official selling rate of Cr$18.82 and Cr$51.18 surcharge). Also, in accordance with a special arrangement, the rate of Cr$18.82 that had applied at the end of 1957 to all newsprint imports was depreciated to Cr$22.82 for one class of newsprint and Cr$28.82 for another class (for details of this arrangement and of subsequent adjustments in the special rate for newsprint in August 1958 and in January and February 1959, see Part II, page   ).

As part of the general coffee program, the variable coffee bonus was increased from July 1, 1958, resulting in a depreciation of the effective rate of coffee export proceeds from Cr$43 to Cr$54 per U.S. dollar. At the same time, exports of cocoa cake were moved from the Cr$43.06 rate for cocoa and its derivatives (Category II) to the Cr$92 rate for Category IV exports. A further depreciation occurred on October 4, 1958 when some export products in Category III (Cr$70 rate) were moved to Category IV (Cr$92 rate), and the proceeds of all exports not listed in the four categories were shifted to the free market. On the import side, the two preferential import categories and the relative Cr$58.82 and Cr$70 rates were merged at a single rate of Cr$80 per U.S. dollar.

On January 10, 1959, the variable bonus arrangement for coffee exports was eliminated altogether and a rate established of Cr$60 per U.S. dollar (i.e., Cr$18.36 plus a bonus of Cr$41.64); prior to this, the effective rate had been about Cr$50 per U.S. dollar. Also, the rate for Category II exports (cocoa beans and derivatives) was moved from Cr$43.06 to Cr$70 per U.S. dollar (i.e., Cr$18.36 plus a Cr$51.64 bonus), and a new Category III was established (comprising all products formerly receiving rates of Cr$70 and Cr$92 per U.S. dollar) with an exchange rate of Cr$100 per U.S. dollar--i.e., Cr$18.36 plus a bonus of Cr$81.64. Authority was given for proceeds of all exports not classified in the three categories to be negotiated in the free market. As a result of the increases in the export bonuses, the surcharge on payments for preferential imports was raised from Cr$61.18 to Cr$81.08, making the new effective rate Cr$100 per U.S. dollar--the official selling rate had been changed to Cr$18.92 per U.S. dollar on January 3, 1959 by virtue of an increase in a stamp tax.

During 1958 there were changes in the amounts offered at auction of convertible and other currencies, depending on the exchange availabilities of the currencies. In the case of convertible currencies, the general practice has been to adhere for as long as possible to a fixed allocation. For many other currencies the amount offered for auction has been varied more frequently, in line with the Bank of Brazil's position in that currency. The Bank of Brazil was authorized by the Council of the SUMOC on August 26, 1958 to offer at auction unlimited quantities of those bilateral currencies in which Brazil maintained credit balances. Accordingly, this arrangement now embraces bilateral currencies with the following countries: Bolivia, Chile, Czechoslovakia, Denmark, Finland, Hungary, Iceland, Israel, Norway, Poland, and Spain. Since the last consultations the Brazilian authorities have maintained some measure of flexibility in the minimum bid policy for these and other bilateral currencies (except those of East Germany, Rumania, and Yugoslavia) in an effort to reduce the credit balance of the relative bilateral accounts, and minimum bids have recently been set at about 70-75 per cent of the actual bids for the U.S. dollar during the previous week for the General and Special Categories. In accordance with the terms of new payments agreements concluded during 1958 with East Germany, Rumania, and Yugoslavia, minimum bids for the clearing dollars relative to those agreements were set at the same level as the bids for the U.S. dollar.

Following the establishment of nonresident convertibility by the European members of the Hague Club, auctions of ACL dollars were combined with auctions of U.S. dollars on January 14, 1959, and exchange certificates denominated in U.S. dollars are now freely transferable into any of the externally convertible currencies of the former ACL area.

An indication of the rate depreciation since December 1957 is given in the following table which shows the average agios for the U.S. dollar (120 days' delivery) in the various auction markets, and also the average surcharges on preferential import payments, during each of the months listed--the effective rate results from the addition to the official rate of the agio or surcharge as applicable. The free market rate quotations of the commercial banks at the end of the months shown are also given for purposes of comparison.

	Cruzeiros per U.S. dollar				
	December 1957	June 1958	December 1958	January 1959	March 10 1959
General Auction	66.79	131.15	186.99	223.37	278.00 1/
Special Auction	226.22	287.59	301.00	350.71	342.00 1/
Specific Auction	32.84	45.56	62.41	89.05	n.a.
Preferential Imports	28.10	38.86	61.18	74.65	80.00 2/
Free Market					
Buying	89.30	131.50	136.50	142.50	141.50
Selling	91.30	134.50	140.50	146.50	145.50

1/ Rio de Janeiro market only.
2/ Estimated.

The level of the free market rate from the beginning of the second semester of 1958 appears to have been influenced by the volume of export proceeds permitted to be transacted through that market. The authorities estimate that the receipts from about one thousand products are now effected at the free market rate and should amount to the equivalent of about US$60-70 million in 1959. In value terms, the principal free market exports in 1959 are expected to be manufactured goods (about US$30 million) and processed meats (about US$12 million). Other significant items will be chemicals and pharmaceuticals (about US$8 million), rice (about US$7 million), and essential oils (about US$5 million). The Brazilian authorities indicated that they have not intervened in the free market and that it is not their policy to do so.

Since the last consultations about 50 items, most of which were industrial chemicals, have been transferred from the Special Category import list to the General Category. During the same period, two transfers have been authorized from the General Category to the Special Category; one was in respect to items stated to have been incorrectly included in the General Category in the first instance, and the other was potassium nitrate for agricultural use which was transferred to the Special Category in order that it could be included in the Specific Auctions for fertilizers. It is the general policy of the authorities not to approve requests for transfers from the General to the Special Category for protective reasons, and in fact many requests for transfers to the Special Category have been rejected during the past year.

During 1958, Brazil entered into several new bilateral trade and/or payments agreements. Agreements signed with East Germany (September 1958) and Rumania (July 1958) raised to five the number of Eastern European countries with which Brazil maintains bilateral arrangements. These two agreements, as well as one concluded with Yugoslavia (April 1958) are each for a period of one year with provision for automatic extension. Current transactions under the agreements will be settled in U.S. dollars, and it is provided that Brazil will extend to export receipts and import payments through the accounts exchange treatment equal to that granted to exports and imports paid for in currencies of limited convertibility.

Brazil concluded a new trade and payments agreement with Japan in October 1958 (for a minimum period of one year and with provision for automatic extension) on the basis of payments between the two countries being effected in external account sterling. Subject to ratification by the parties, Brazil also entered into a new three-year trade and payments agreement with Bolivia in March 1958 providing for settlement of commercial transactions in cruzeiros and/or bolivianos.

In line with the form of the ~~model~~ Montevideo payments agreement, Brazil concluded new payments agreements in U.S. dollars with Argentina, Chile, and Uruguay in September 1958 (the latter agreement is awaiting ratification). The agreement with Argentina is for a period of three years and those with Chile and Uruguay for two years, with provision for automatic renewal of each agreement. The Argentine and Uruguayan agreements provide that, when the balances of the accounts are in excess of stated amounts, the creditor will have the option of requesting the transfer of all or part of the surplus to clearing accounts with other Latin American countries. In the case of the agreement with Chile, it is stipulated that the amount in excess of an agreed working balance will, at the request of the creditor, be transferred to another Latin American clearing account; transferred to a clearing account with a third country (not American); paid in another currency; or paid in freely convertible U.S. dollars. Each of the three agreements stipulates that the partner country will ensure that agreement dollars may be converted into the currency of the other country at rates of exchange effective in the two countries for the same operations effected in freely convertible U.S. dollars.

The Brazilian authorities hope that the conclusion of these three agreements, with clauses providing for transferability of balances, as well as the negotiation of similar agreements between other countries in Latin America, will make possible the introduction in that area of a system of multilateral clearing of bilateral balances, as a forerunner of a future Latin American common market. The various aspects of the subject are currently being studied by representatives of the countries concerned in consultation with the U.N. Economic Commission for Latin America.

In view of the establishment, at the end of 1958, of the external convertibility of their currencies by the European members of the Hague Club, the necessity of separate treatment of those currencies under the Brazilian auction system disappeared and, as noted above, the auctions for these currencies and the U.S. dollar were merged in January of this year. Representatives of Brazil and the European countries participating in the Hague Club arrangements have recently met in London to consider the implications of the new currency arrangements in Europe for future trade and financial relationships between those countries and Brazil. It was stated later that members of the Hague Club (in future referred to as the Brazil Club) would meet together from time to time to discuss the promotion of greater trade between Brazil and Western Europe.

c. The present system. ~~Despite the developments of the past year, as reviewed above, it is apparent that there has been no significant change during the period in the complex nature of Brazil's multiple rate system. This factor has its reflection in the spread of rates at which the various trade transactions in Brazil are currently effected~~. For exports, the range is from the Cr$60 rate for coffee to the free market rate of about Cr$140 per U.S. dollar for minor exports; in the case of imports, the spread is from Cr$43.24 for one class of newsprint to about Cr$360 per U.S. dollar for Special Category goods in the auction market. (A table of effective exchange rates is given in Part II, p. .) It is also noteworthy that Brazil has entered into additional bilateral trade and payments agreements since the last consultations. The following sections provide a brief statement of the current restrictive system in Brazil.

(1) Imports. Apart from the special arrangements mostly involving foreign financing, there are two basic methods for effecting import payments in Brazil: (a) at fixed preferential exchange rates resulting from the addition of fixed surcharges to official rates and within global exchange quotas; and (b) through exchange auctions held periodically for various currencies. Imports licenses are required for the import of goods in a Special Category and for a few other specified (including preferential) imports, but licenses for Special Category imports are understood to be freely granted to holders of exchange certificates purchased at auction, while those other imports which require import licenses are authorized within global quotas established in an exchange budget.

Most preferential imports are currently subject to an effective rate of Cr$100 per U.S. dollar. Imports of newsprint continue at special rates resulting from the addition to the official rate of surcharges that are increased every six months--at present there are two rates of Cr$43.24 and Cr$79.73 per U.S. dollar. A special preferential exchange rate treatment is extended to imported component parts of automobiles for assembly in Brazil, in connection with the development of the Brazilian automobile industry (see Part II, p.). The present preferential treatment is to remain in force until June 30, 1959; subsequent arrangements are at present under discussion between the authorities and representatives of the automobile industry.

Importance?

Payments for all other imports are transacted through auction markets. These imports are classified in two categories--a General and a Special Category, the composition of both being generally as they were in November 1957. Automobiles with a value of more than US$3,500 are prohibited imports. An exchange certificate or certificate of exchange cover must be purchased at auction for commodities in either category. Separate auctions are held for the U.S. dollar, for each of the currencies of the countries with which Brazil has bilateral payments agreements, and for specific commodities (fertilizers, insecticides, and fruit, under bilateral agreements, and automobiles below a stated value). Minimum bids are established for most bilateral currencies auctioned, and these have been about 70-75 per cent of the actual bids for the U.S. dollar for the General and the Special Category during the previous week. Effective rates in terms of the U.S. dollar in auction markets in Rio de Janeiro on March 10, 1959 were about Cr$297 for the General Category and about Cr$360 for the Special Category.

(2) Exports. Exports are now classified in three categories, each with a separate exchange rate--viz., for Category I (coffee beans), Cr$60 per U.S. dollar (official rate plus a bonus of Cr$41.64); for Category II (cocoa beans and derivatives), Cr$70 per U.S. dollar (official rate plus a Cr$51.64 bonus); and Category III (miscellaneous products including sugar and cotton), Cr$100 per U.S. dollar (official rate plus a bonus of Cr$81.64). However, the proceeds of all exports not listed in the three categories are negotiated in the free market, and include manufactured goods, processed meats, chemicals, and pharmaceuticals.

Export licenses are required for all exports except coffee. The export of coffee is authorized by the Brazilian Coffee Institute. Proceeds of exports, other than those permitted to be negotiated in the free market, must be surrendered to an authorized bank, but mining industries may retain abroad 30 per cent of their export proceeds to service registered loans.

(3) Free market. All capital transactions and transactions in invisibles not connected with trade are effected through the free market. In addition, as noted above, exchange proceeds of exports not specifically listed in any of the three categories of exports may be negotiated in the free market. The commercial bank selling rate at mid-March 1959 was about Cr$145.50 per U.S. dollar.

(4) Bilateral arrangements. Brazil maintains bilateral payments and/or trade agreements with 18 countries--four Latin American countries (Argentina, Bolivia, Chile, and Uruguay); seven European countries (Finland, Iceland, Norway, Portugal, Spain, Turkey, and Yugoslavia); five Eastern European countries (Czechoslovakia, East Germany, Hungary, Poland, and Rumania); one Middle Eastern country (Israel); and one Far Eastern country (Japan). Besides these agreements, Brazil has bilateral relationships on a de facto basis with Denmark and Sweden. The value of trade with countries with which Brazil maintains bilateral arrangements represented 26 per cent of Brazilian exports and 20 per cent of her imports during 1958. The agreements are of particular significance for Brazil's trade with Latin American countries. In 1958, almost all of Brazil's exports to Latin American countries were to Argentina, Bolivia, Chile, and Uruguay, with which countries trade and payments agreements are maintained, while nearly half of Brazil's imports from Latin American countries in 1958 were from the same four countries.