THE WHITE HOUSE

WASHINGTON

September 3, 2009

Dear Colleagues,

Ahead of our meeting in Washington, I am writing to share our views on the agenda for the Pittsburgh Summit.

At the G-20 Leaders' meeting in April, our countries agreed to do whatever it took to support recovery and strengthen financial supervision and regulation so that a crisis of the current magnitude does not recur. In Washington, we should take stock of progress fulfilling those commitments and discuss what we aim to achieve in Pittsburgh. In Pittsburgh, we hope the G-20 will seize the opportunity to shape the global economic and financial system in the wake of the crisis. We should aim to adopt a policy framework to achieve sustainable and balanced growth; promise to prioritize jobs and policies to equip our people for the 21st century economy; commit to further actions to strengthen the global financial system; reach agreement on bringing governance and missions of the international financial institutions into alignment with key post-crisis priorities; support initiatives on food security, financial access and energy in the world's poorest countries; reiterate our commitment to maintaining economic openness, set the contours of a financing framework for climate change and agree to strengthen our energy security by increasing energy market transparency and by committing to eliminate non-needs based fossil fuel and electricity subsidies.

The Global Economy

Since April, clear progress has been made. G-20 output increased in the second quarter of 2009, albeit modestly, and growth is expected to accelerate in the second half of the year following a sharp contraction in the first quarter. The International Monetary Fund (IMF) is projecting collective G-20 growth in 2010 of 3.2 percent, compared with an overall contraction of 1.1 percent in 2009. In addition, stresses in financial markets have abated significantly; global equity markets have risen about 35 percent since the end of March; credit market issuance globally has passed $1 trillion this year; and indicators of credit risk have fallen substantially since March 31. Our financial institutions are more resilient and more successful in raising capital. This progress reflects the unprecedented policy actions taken by G-20 countries to provide macroeconomic policy support and extraordinary intervention in our financial systems.

Despite the positive signs in recent months, risks remain: private sector demand is expected to remain weak as rising unemployment in most of our economies weighs on income growth, and some credit markets remain constrained. As the IMF has noted, the overarching risk is a stalled recovery. The continuation of supportive fiscal, monetary, and financial policy measures will be essential in helping to secure a durable recovery. Prematurely withdrawing support risks a return to recessionary conditions and instability in financial markets.

In the period ahead, G-20 countries will need to prepare to unwind the extraordinary support measures put in place to overcome the crisis at a pace that is appropriate to the particular circumstances of each economy. Already, there is considerable variation across our economies in the strength of demand and the health of our financial systems. For all G-20 countries, however, the speed of the withdrawal of the fiscal and monetary policy stimulus and of financial sector support should be undertaken at a pace and in a manner to avoid jeopardizing either individual country and financial sector recoveries or the recovery of the global economy and financial system.

Framework for Sustainable and Balanced Growth

As recovery is established, we need to have in place a new framework that will support a healthy and vibrant global economy. The United States has circulated a draft Framework for Sustainable and Balanced Growth that we would like to reach agreement on and announce in Pittsburgh. The Framework would be a pledge on the part of G-20 Leaders to individually and collectively pursue a set of policies which would lead to stronger, better- balanced global growth. This could concretely demonstrate our commitment to the values in the draft Charter for Sustainable Economic Activity.

G-20 countries should pledge to run responsible fiscal policies, strengthen financial supervision, promote more balanced trade, support open trade and investment, undertake monetary policies consistent with low and stable inflation, and undertake structural reforms of their labor, product, and capital markets to increase their potential growth rates and facilitate the expansion of domestic demand. As private and public saving rises in key G-20 external deficit countries – a necessary process that is already underway – the world will face lower growth unless other G-20 countries undertake policies that support a shift towards greater domestic, demand-led growth. Achieving a sustainable rebalancing of demand will require structural reforms that increase the weight of private domestic demand and strengthen long-run growth potential.

The Framework proposes creating a forward-looking G-20 peer review process to assess members' policy frameworks and their collective implications for global growth. The IMF would be at the center of this process through its analysis, tasked with providing semi-annual assessments on the basis of candid, independent, and transparent surveillance of whether trajectories of demand, reserve, debt, credit, and balance of payments are balanced and sustainable.

Prioritizing jobs and equipping our people for the 21st Century economy

The impact of the crisis on workers has been particularly severe. As growth returns, we need to do everything we can to ensure that employment does as well. The G-20 should commit to implementing recovery plans that prioritize job growth, income support for the unemployed, and the quick regaining of employment.

Each of our countries also will need, through its own national policies, to equip its workforce to succeed in the integrated global economy. We all need to strengthen the ability of workers to adapt to changing market demands and to prepare our workers to benefit from new investments in the areas of clean energy, heath and infrastructure. We should pledge to support robust training efforts in our growth strategies and investments, welcome the recently-adopted ILO's Global Jobs Pact and commit to hold the first G-20 Labor Ministerial in 2010.

Strengthening the International Financial System

Substantial progress has been made on the commitments made in Washington and London to improve financial supervision and regulation. In London, we reached consensus on a global framework of reform. We can point to many accomplishments, including: an expanded scope of regulation to include previously under-regulated institutions, markets, and products; strengthened prudential oversight and enhanced regulation through higher capital requirements on risky assets and off-balance sheet items; improved risk management, with guidelines on liquidity risk management; strengthened financial integrity, by bolstering international standards in three areas – tax information exchange, anti-money laundering/combating the financing of terrorism, and prudential oversight – through expanded use of peer-review mechanisms to measure and promote compliance with standards; and strengthened international cooperation through expansion of the membership and mandate of the Financial Stability Board.

Our challenge now is to put the framework in place. Each of us now needs to implement these reforms at the national level, in a consistent way that ensures an international level playing field, and we should commit to do so by the end of 2010. As part of this, G-20 Leaders should commit to reach agreement on an international framework of reform in the following critical areas:

1. *Building high quality capital and mitigating pro-cyclicality*: We should implement higher quality capital requirements, a simple leverage ratio, counter-cyclical capital buffers, and forward looking provisioning. We should also implement specific liquidity risk requirements. Our standards for systemically important financial institutions should be even higher.

2. *Compensation reform*: We each need fairer and more transparent compensation structures for senior executives at our major financial firms aligned with sound risk management and long-term value creation. We should implement reforms that strengthen disclosure and accountability to shareholders and greater board independence in the pay-setting process.

3. *Improving over-the-counter derivatives markets*: All standardized OTC derivative contracts should be traded on exchanges or electronic trading platforms and cleared through central counterparties. Non-standardized derivative contracts should be reported to trade repositories and, if not centrally cleared, should be subject to higher capital requirements.

4. *Cross-border banking resolution*: We should develop resolution tools and frameworks for the effective resolution of financial groups to help mitigate the disruption of financial institution failures in the future.

Modernizing global financial institutions to reflect the 21st century global economy

The challenges posed by the crisis have highlighted the need to improve our multilateral cooperation in order to further promote global financial stability, foster sustainable development, and lift the lives of the poorest from poverty. Modernizing the international financial institutions and the global development architecture will be essential.

International Monetary Fund

In London, we committed to substantially increasing resources available to the IMF so it could fight the spread of crisis in emerging markets and developing countries. These efforts, coupled with innovations in IMF facilities, significantly contributed to lessening global risks. Capital is again flowing to emerging markets. In particular, our London commitment to allocate $250 billion in Special Drawing Rights to IMF members has already been fulfilled. We also agreed to expand and enlarge the IMF's New Arrangement to Borrow (NAB) by up to $500 billion; while substantial bilateral financing has been mobilized, these resources have not yet been incorporated into the NAB. By Pittsburgh, the G-20 must make good on this pledge.

Alongside its central role in fighting the crisis, the IMF's mission must be modernized and its governance structure reformed to maintain the institution's central role in promoting global financial stability and rebalancing growth. There are several key priorities that must be addressed to make this happen.

- It is critical to further strengthen IMF surveillance. The G-20 should endorse the IMF's role in supporting efforts to achieve more sustainable and balanced growth by providing candid, independent, and transparent surveillance of country policies.

- The G-20 should support the IMF's essential role in providing precautionary resources so that private capital continues to flow to its members, lessening the adjustment burden on individual countries and the perceived need for excessive reserve accumulation, and in supporting world growth.

- The G-20 should welcome IMF measures to strengthen its lending facilities to help countries insure against financial volatility.

- In order for the IMF to remain legitimate and more effectively fulfill its mandate, reform of its governance structure is imperative. At Pittsburgh, the G-20 should call for a shift in the range of five percent in quota share for dynamic emerging market and developing countries as part of the next quota review to be completed by January 2011. The G-20 should also call for a smaller IMF Executive Board that will preserve the chairs held by emerging market and developing countries.

Multilateral Development Banks

The multilateral development banks (MDBs) have played an essential role in helping to mitigate the impact of the crisis on the world's poorest. The G-20 should affirm our commitment to provide adequate resources to the MDBs – in particular by taking steps to avoid a disruption of concessional financing to the most vulnerable countries.

Looking ahead, the MDBs should play a central role in the provision of critical public goods in the 21st century, and should orient their missions around four critical priorities: 1) facilitating the transition to low-carbon economies; 2) building food security through enhanced productive capacity in agriculture; 3) providing support for private sector-led growth and infrastructure; and 4) strengthening human development and security in the most challenging environments.

The G-20 should assess the capital adequacy of each institution on the basis of a demonstrated ability to fulfill these four priority missions and five principles of reform: 1) a clear division of labor that reflects the relative strengths of each institution; 2) an increased commitment to transparency, accountability, and good governance; 3) the ability to both innovate and expand capacity to achieve demonstrable results; 4) strong analysis of future demand; and 5) greater attention to the needs of the poorest countries.

Strengthening Recovery in the World's Poorest Countries

Recognizing the special challenges faced by the world's poor, the G-20 should signal its support for investing in long-term food security, reducing energy poverty, and improving financial access, both for small enterprises and poor households currently outside the financial system.

Food security: To advance agricultural productivity and food security for the world's poorest, G-20 Leaders should call for the creation of a multi-donor agriculture and food security trust fund at the World Bank that would help strengthen donor coordination in support of country-owned agricultural development plans.

Energy poverty: To reduce energy poverty, while simultaneously increasing energy security and protecting both the local and global environments, we would like to see increased bilateral funding and contributions to the Scaling-Up Renewable Energy Program at the World Bank.

Financial Access: To expand financial access, the G-20 should work together to promote successful policy approaches to new modes of financial service delivery capable of reaching the poor and scaling up the best models of small- and medium-sized enterprise finance.

As we take these steps to increase the flow of capital to developing countries, we also need to prevent its illicit outflow. We should work with the World Bank and others to stem these flows and to secure the return of stolen assets to developing countries.

An Open Global Economy

The G20 should reiterate its stance against protectionism and continue to press for progress on trade liberalization, including with regard to the Doha negotiations. We will await the results of the meetings in India this week to determine an appropriate outcome related to this issue.

Climate Change

As the largest global economies, it will be critical for the G-20 countries to demonstrate a commitment to addressing climate change and respond forcefully to the challenges it poses. We have a significant role to play in helping to develop a practical and effective international financial framework for climate cooperation that can support negotiations and achievement of an agreement in Copenhagen. We recognize that climate finance needs to be scaled up significantly, but it must work hand-in-hand with development assistance and private sector incentives to be effective and efficient. This implies a critical role for the MDBs. Therefore, we need to work together to increase public finance delivered through multiple channels, to coordinate climate finance with development assistance, and to leverage the private sector through improvement, expansion, and oversight of carbon markets.

Energy security

Both producers and consumers can be negatively affected when energy markets work inefficiently. G-20 Leaders should commit to improving energy security by increasing oil market transparency, including by reporting comprehensive data on domestic oil markets and taking steps to oversee the OTC markets so that regulators have a more complete view into the actions of market participants.

Eliminating fossil fuel and electricity subsidies would help energy markets work better and improve our energy security. It also is a logical step in combating global climate change, as it would encourage energy conservation, and facilitate new technologies. The move away from subsidies should be managed to protect those most vulnerable to price increases. The G-20 should commit to take the lead in eliminating non-needs based fossil fuel and electricity subsidies and to provide technical assistance to non-G20 countries taking steps to reduce fossil fuel and electricity subsidies.

I look forward to your feedback on these issues in Washington and to making the Pittsburgh Summit an important success.

Sincerely,

Michael Froman