G20
Pete Sepp
NTU
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Operator: Good day, everyone, and welcome to today's program. At this time, all participants are in a listen-only mode. Later, you will have the opportunity to ask questions during the question and answer session. You may register to ask a question at any time by pressing * and 1 on your touchtone phone, and you may withdraw yourself from the queue by pressing the # key. Please note this call may be recorded. I'll be standing by should you need any assistance.

It is now my pleasure to turn the conference over to Mr. Pete Sepp, National Taxpayers Union. You may begin, sir.

Pete Sepp: Thank you very much and thanks to everyone who's participating in the call. We are sure that you will find this new report of interest.

Back in 2012, Mr. Glassman and Mr. Brill joined with National Taxpayers Union to produce a study called "Who should the '20' be? A new membership system to boost the legitimacy of the G20 at a critical time for the global economy." Well, two years later, certainly the critical time for the global economy remains with us. Events may have changed perhaps in Argentina, the Crimea region, and the Middle East with their potential to disrupt worldwide economic as well as political conditions, but the central question remains: what kinds of institutions are best suited for providing the nimble response we need for global financial stability? That's why my organization has an interest in this question. We believe that the older institutions such as the United Nations and the International

Monetary Fund are following bureaucratic models that tend to resort to higher burdens for taxpayers not only in the United States but abroad. We take a great interest in the international movement for limited government through an association called World Taxpayers Associations.

The entire point of this paper from my perspective at National Taxpayers Union is to recommend a better approach: a new model of cooperation that can provide that kind of international financial stability without the baggage, as the authors call it, the operational baggage of other entities such as the IMF and the United Nations. This updated paper is providing a somewhat different methodology than the previous paper; tweaked, if you will. And the results although not as extreme variance with what they were able to conclude in 2012 provide an encouraging I think way to consider how G20's membership criteria can be strengthened to the point where it is more transparent, more accountable, more legitimate. Those are the kinds of principles we're going to have to establish to a greater degree to make the G20 realize its full potential.

So, I will transition now to one of our study's authors, James K. Glassman, who will give an overview of some of the findings of the study. He was formerly U.S. Undersecretary of State for Public Diplomacy and Public Affairs, CEO currently of Public Affairs Engagement, a visiting fellow at American Enterprise Institute, and member of the Investor Advisory Committee of the SEC.

Thank you for joining us, Jim, and please take it away.

James K. Glassman: Thank you, Peter, and let me just say at the onset that I speak on my own and not as a member of the SEC's Advisory Committee.

The finance ministers meeting over the weekend in Cairns, Australia of the G20 issued a communiqué that made it very clear that the global economic and financial system have not recovered from the crisis of 2008 and 2009 yet, and now it's been six years. The G20, the only or the main global organization dedicated to be the locus of reform, stability, and growth is suffering what we believe to be a crisis of confidence and one big reason is a lack of legitimacy involving membership. Who gets to be a member of the G20? Well that's a good question and the answer is it is largely arbitrary.

Since its founding in the wake of the Asian financial crisis in 1999, the G20 has operated without transparent rules; in fact, without any rules all governing which countries are members. We have taken it upon ourselves, Alex Brill, my AEI colleague, and I to ask two questions. If the G20 had objective standards for membership, what should they be; and under those standards, who should be granted G20 membership?

As Peter said, this was an exercise that we embarked upon two years ago and unfortunately in the two years since we issued our original report, the situation for the G20 has only become worse. Argentina and Russia, which were identified as ill-suited for membership in the G20, have continued on paths that deviate sharply from international norms.

Alex Brill is going to talk to you about how we decided on the metrics that we chose, but let me just go straight to the bottom-line and tell you what the results of the application of those metrics is. Four current G20 countries should not qualify for membership in the G20 under our criteria and they are, in alphabetical order: Argentina, Indonesia, Russia, and

Saudi Arabia. Four current nonmembers should replace them and they are: Chile, Norway, Singapore, and Switzerland. I should say that we made a decision that we would keep the E.U. as a member and that the current four E.U. country members: UK, France, Germany, and Italy; would remain as country members but there would not be any other E.U. country members. Norway and Switzerland are non-E.U. country members. One can argue with that but we spent a lot of time and made that decision.

We also assumed a rule on representation from the five major geographic regions in the world and one country, South Africa, qualifies because of that rule; otherwise, Russia would occupy the 20^{th} spot.

Just, I want to put some special stress on Argentina. As in 2012, Argentina finished in last place overall among current members of the G20. It was also last in GDP, last in imports, last in exports, third to the last in control of corruption, last in regulatory equality, next to the last in rule of law, and last in a tie for three others in systemic connectedness – and these are criteria that Alex is going to explain in a second – and among a list of countries with the median score of 60.5 points, Argentina's score is 14.1. Argentina really stands out as a country that never should have been on the G20 in the first place and clearly should not be on today under any objective criteria.

Now I'm going to turn to Alex Brill who is a fellow at the American Enterprise Institute and my collaborator in this endeavor to explain further what we've done.

Alex Brill: Thank you, Jim, and thank you, everyone, for joining this morning. Let me just take a few minutes to step a bit into the weeds and talk about the methodology and the data that were applied.

As Jim described, our view is that the membership process for the G20 should not be random. It should be reasoned and logical, and that it should be a data-driven process based on two things generally. One is to identify the goals and objectives of the G20 and then identify appropriate data that match those criteria, those goals and objectives, and apply that process to therefore determine which countries would be best suited to represent the global economy in the G20 and help this organization in its goals.

The process began by trying to determine what the objectives are for the G20. Here, we did not try to come up with our own objectives of what the G20 should be focusing on, but rather we looked to the actual statements made by the G20 heads of states when they came together in the wake of the financial crisis in 2008. Those three objectives were: restoring global growth, strengthening the international financial system, and reforming international financial institutions. Those were the goals set forth by the G20 itself.

Our next step is to identify data that we think are reliable and appropriate that would correlate and help predict the ability of countries to work towards those objectives. We think that the following three broad categories of data meet that bill. First, a country's economic size and global trade activity; second, the country's adherence to the rules of law and other principles consistent with market-based economies; and finally, financial interconnectedness. Given the fact that the G20 is so focused on the international financial system and reforming international financial institutions, we thought this variable would be particularly appropriate; one that measures a country's financial services sector, its size, and the magnitude of its inbound and outbound banking activities, the degree to which its banking center is connected to the global economy. Those were the three goals that we identified; those were the three categories of data that we identified.

We then applied those criteria in identifying specific data sets that would meet these objectives and so I can roll through those relatively quickly. For the first one, a country's size, we focused on GDP, exports and imports; to measure the country's commitment to the rule of law, we looked to the World Bank and a program operated inside the bank that evaluates each country on three metrics: corruption, regulatory equality, and rule of law gives scores to each of the countries for each of those three measures; and then finally, to measure a country's financial interconnectedness, it's sense of financial sector's role in the global economy. We turned to the IMF and a process that they have ongoing called the Financial Sector Assessment Program, FSAP, which on a regular basis is examining countries and their financial market sector. That metric as Peter alluded to is slightly different than it was in our original paper as the IMF has continued to make progress on making these determinations. They have made some adjustments to their terminology. We think that that data is now more informative as they have become more educated in making that determination.

We take these seven variables and assigned a score to each one of them. The countries that have the highest score in any given category is given a score of 100. So for example for GDP, the United States is given a score of 100. A country that has an economy that is 20% as large as the United

States would be given a score of 20. Similarly, we apply a similar process for each of the seven variables. At the end, these seven variables are simply averaged, given equal weight and a final score is determined.

As Jim noted, we include the European Union in this process though we don't have scores for them, but excluding the European Union, the United States scores first at 95.5 points and last on the list, the 20th is South Africa with a score of 26.2. As Jim noted, there are as a result of this process four countries that we would suggest join and four countries that we believe are inappropriate, most notably Argentina and as well as Indonesia.

That's [it on] the methodology. Let me turn it back to Pete and we can take it from there.

Pete Sepp: Yes. Thank you both, Jim and Alex. Excellent briefing, excellent overview. Any questions from participants in the call at this point?

Operator: At this time if you'd like to ask a question, please press * and 1 on your touchtone phone, and you may withdraw yourself from the queue at any time by pressing the # key. Once again if you'd like to ask a question, please press * and 1 on your touchtone phone. We will now pause to allow questions to enter the queue. [Pause]

Mr. Sepp, seeing no further questions, I will turn the conference back over to you for closing remarks.

Pete Sepp: Yes. We have a couple of questions, of course, that we can discuss here and especially with the release of this communiqué from the finance ministers, you had a comment to offer, Jim?

James K. Glassman: Yes. Actually, I have a question that I would ask if [Laughter] I were asking questions, which [Laughter] is what to do about this?

So we do make a recommendation in the conclusion of our piece, of our study. So the first thing that we say is that the G20 should reevaluate its membership on a regular basis; not have too many years pass but also not do it too often. Our recommendation is to reevaluate the membership every five years which would create a reassurance that current members are deserving of G20 status, that's the legitimacy issue; and providing an incentive for other countries to gain membership by implementing reforms. It's one of the reasons that our metrics do allow smaller countries like Singapore and Norway to become members. We want those countries to aspire to be members and make changes accordingly.

We also believe very strongly that these changes need to be made right away. So the G20 is having its summit in Brisbane November 14th and 15th, we think that is the time to adapt these criteria and that the actual changes ought to be made during 2015.

Pete Sepp: Yes. So operationally, this is not all that difficult of a change to make.

James K. Glassman: No.

Pete Sepp: There's no real bureaucratic process that has to be gone through here, these can happen virtually right away.

Alex Brill: That's one of the strengths of the G20. So while we are certainly here offering criticism today, there are strengths to the G20 and one is its ability to change course if it chooses to. It was brought together very quickly in the wake of the Asian financial crisis and reconstituted with more vigor in the more recent financial crisis in 2008, and it doesn't carry the baggage that we refer to in the paper that some of the other global institutions carry and therefore could make this change relatively quickly.

Pete Sepp: So that sort of prompts another question, why keep it at 20? Why should the membership remain at that figure? Why not 40, 50, 100?

Alex Brill: Well, there's certainly nothing magic about the number 20. Arguably, this is the G19 plus the European Union, and one could even make the case that it could be G21 or something like that. To your specific question, why not the G50, G100, or G-everybody? I think it becomes quite unwieldy as it becomes much larger and I think that the underlying framework is that the finance ministers on a regular basis and the heads of state from time to time get together [a roundtable] where they can see each other eye to eye, that there are personal dynamics that are in play and leadership roles that are required for those countries that are scoring the highest by the metrics that we think are most appropriate.

Pete Sepp: So, in the two years since the last report was generated and now we have a new one, how precipitously has G20's position as a legitimate institution fallen because of lack of action on these kinds of standards? Are we at a crossroads here for the institution?

James K. Glassman: Well, I think we are. I mean the G20 has made progress in certain areas and not in others. The most important areas where it has not made very much progress has been in encouraging economic growth and if you look at the communiqué from the finance ministers, the first 5 of the 10 items have to do with economic growth and they say that "we need to grow by an extra two percentage points by 2018." Well, that doesn't sound like much but it's [Laughter] a lot.

Pete Sepp: It is.

James K. Glassman: We've also seen that the G20 members themselves have not complied with the targets that were set by the organization itself, specifically China, Saudi Arabia, and Argentina have been very much derelict in this respect.

So, the G20 is really not doing its job or certainly not what we had expected of and I think the – I would say that the results are kind of mixed when ti comes to financial stability. Even there, we still don't have rules on "too big to fail," which is I think the real key.

So there's a lot more to be done and you can criticize the specific steps they have taken. We are focusing on just one thing, which is legitimacy as it is tied to membership, and one of the things about our paper is that we go into a fair amount of detail about academic research that has linked these two: legitimacy and membership. We also refer to a study that also advocates a change of membership. We don't agree with those conclusions of that study, but the fact is there are a lot of people who are very interested in making these changes. I think that the word that I used earlier, crisis, is an accurate one; crisis of legitimacy.

Pete Sepp: Very good. So, we have the possibility of these standards being adapted in November and of course you point out these criteria are not necessarily the only ones that the G20 could adapt, but I'm trying to think of what could possibly be better than these three with a formula the way it's balanced? If you were able for example to find out more data, create some other kind of statistic, what other possible evaluative method would be included in this, if any?

Alex Brill: I mean it's certainly the case that there is nothing absolute about these seven metrics that we picked. The G20 could pick others. They could create their own metric based on given criteria. They could conduct surveys of the countries and create their own lists, and they could alter the weight for these variables. We weighted each variable equally in this process. That seemed simplest and fairest, but they might say that the GDP is more important than imports or something like that.

I think one of the key points, however, is that if you were to chose other data that are in the same framework, the same notions of matching up to the stated objectives and goals of the G20. So if you were to pick other data that represented economic size, trade, rule of law, and had a focus on the financial sectors, you would get virtually identical results. By that I mean you would get of the 20, you would certainly get 14, 15, 16 of these countries consistently making the list. When you get down to the 17th, 18th, 19th and 20th spot of the G20, it's a little bit more difficult to determine who is the most appropriate. We saw some slightly different results this time than we did when we looked at these two years ago and so you'd have a little bit of movement in and out. As Jim described earlier, I think that's positive that countries could if they worked towards this goal could earn membership at the next round. Similarly for countries who are in, if they don't continue to make progress, they might slip out. So that's a positive incentive.

Pete Sepp: But there is however very little hope under any statistical matrix of Argentina being included.

Alex Brill: Well that's absolutely right. Their score is nowhere near the breakpoint, the cut point for making it in. That was the case this year in our analysis and that was certainly the case two years ago when we asked this question. They are not one of the countries that are on the bubble, near admissions by any regard.

James K. Glassman: Yes and I think the other change that you could make is that kind of geographical balance change, which we have our rules for that, but you might revise them to some extent. For example, you could say there needs to be a Middle Eastern country and that would be Saudi Arabia or that maybe there needs to be two African countries or right now there are three Latin American countries. That's probably about right.

So, you could do that but as Alex says, it's hard to think of how you would change either the weightings or the particular criteria and come up with a result that's very much different from what we have. Not to gang up on Argentina but I would also just to be – but it is such an outlier here.

Cristina Kirchner is giving a speech before the United Nations on Wednesday. This is a country that has defied U.S. Courts consistently, has defied the World Bank, and I really think that a member like this of the G20 really erodes the authority and status of the organization.

You might make the same kind of argument about Russia, although Russia is obviously a very key geopolitical player. It's one of the five permanent members of the U.N. Security Council, but you really want to have as members of the G20 countries that subscribe to the international financial system and that is as absolutely not true in the case of Argentina. Russia actually has complied with the targets that were set years ago for the G20 to a degree that some might be surprised at. They seem to be a fairly compliant country.

So all I'm saying is there may be some changes here and there, but almost any system that you would device will come out with something similar to what we have.

Pete Sepp: Yes.

Alex Brill: Can I just pick up on Jim's first point about the geography, the keeping one country in from each of the five regions? We did as Jim noted go back and forth on that piece of it. That was something that the G20 had advocated for earlier that we chose to keep and I think that there is a sound reason for having that diversity, which is that the decisions that are made by the G20, we want the rest of the world to follow those decisions. We want these countries to be leaders in setting policy to strengthen the global financial system, and it may be the case – now I think it is the case – that countries that are not members of the G20 are likely to follow their local leaders. If the G20 membership was entirely European countries, I think it would be more difficult to get Latin American, South American, or African countries to go along. So I think there's a strong case to have that geography.

I agree with Jim that it may be appropriate to have the Middle East [and] East Asia included as well, and that could be something the G20 itself could consider and therefore Saudi Arabia would be brought in.

James K. Glassman: Yes, I think the main criticism of this if you look at the list would probably be that there are two many European countries. So there's 7 if you included the E.U. as a country out of the 20, but there's no doubt that they deserve to be on the list based on the criteria and you could also even make the argument that "Hey, why isn't Spain on there? Why aren't individual countries that would qualify based on the metrics, why aren't they on?" and I think the answer is because that would make it even more lopsided in Europe's favor.

So, we think a debate about what the metrics ought to be, what the rules ought to be is actually a good one. The problem is currently that the membership system is completely arbitrary and I would just make one more point about that. By having a system of clear criteria, the organization can evolve – and clearly the organization needs to evolve.

We pointed out in the paper that when the G7 itself was formed in the 70's, China was certainly not an economic power and today, if you were to choose seven or five or three countries that were the most important in the world economically, you'd have to include China. So you wouldn't want the G7 as it was currently constituted to have Italy but not China. You need a process that allows that kind of evolution.

Pete Sepp: Yes and a periodic reevaluation of criteria would certainly give you that.

Alex Brill: That's right.

Pete Sepp: Absolutely. Any other questions or comments at this time?

Operator: We have no questions at this time.

Pete Sepp: Alright. I would just remind everyone participating that the full paper, Strengthening G20's Membership is available online at www.ntu – the initials for National Taxpayers Union – ntu.org.

Thanks to everyone for participating.

Operator: This does conclude today's program. You may now disconnect.

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