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# Exploring the Ethical Identity of Islamic Banks via Communication in Annual Reports

Roszaini Haniffa  
Mohammad Hudaib

**ABSTRACT.** Islamic Banks (IBs) are considered as having *ethical identity*, since the foundation of their business philosophy is closely tied to religion. In this article, we explore whether any discrepancy exists between the *communicated* (based on information disclosed in the annual reports) and *ideal* (disclosure of information deemed vital based on the Islamic ethical business framework) ethical identities and we measure this by what we have termed the *Ethical Identity Index (EII)*. Our longitudinal survey results over a 3-year period indicate the overall mean *EII* of only one IB out of seven surveyed to be above average. The remaining six IBs suffer from disparity between the *communicated* and *ideal* ethical identities. We further found the largest incongruence to be related to four dimensions: commitments to society; disclosure of corporate vision and mission; contribution to and management of *zakah*, charity and benevolent loans; and information regarding top management. The results have important implications for communication management if IBs are to enhance their image and reputation in society as well as to remain competitive.

**KEY WORDS:** corporate identity, content analysis, ethical disclosure, Islamic banking, reputation

## ABBREVIATIONS

AAOIFI	The Accounting and Auditing Organisation for Islamic Financial Institutions
ABB	Al-Baraka Bank
ADIB	Abu Dhabi Islamic Bank
ARB	Al-Rajhi Bank
BIB	Bahrain Islamic Bank
DIB	Dubai Islamic Bank
<i>EII</i>	Ethical Identity Index
IB(s)	Islamic bank(s)
KFH	Kuwait Finance House
SIB	Shamil Islamic Bank
SSB	<i>Shari'ah</i> Supervisory Board

## Introduction

*Identity*, according to the Oxford Dictionary, is '(1) absolute sameness; oneness; equality of two expressions for all values of the literal quantities, equation expressing this; (2) condition or fact that person or thing is itself and not something else; individuality, personality' (The Oxford Dictionary, 1984). In terms of *corporate identity*, the consistent visual symbols of the corporation fit the first linguistic definition, while the distinct attributes of the corporation (Balmer, 1998; Bernstein, 1984) or 'the reality and uniqueness of the organization' (Gray and Balmer, 2001, p. 1) fit the second definition. Hence, corporate identity can be 'the same and yet different' (Bernstein, 2003).

A review of the literature on corporate identity indicates a plethora of definitions for the term,

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ranging from the tangible to intangible, and from the tactical to strategic (see Alessandri, 2001; Melewar and Jenkins, 2002 for a compilation of the various definitions). However, there is some agreement among researchers that the term is related to answering the questions “what are we?” and “who are we?” (Balmer and Greyser, 2003) or “what the firm is” (Hawn, 1998; Portugal and Halloran, 1986), hence referring to the distinct attributes of the organisation. Birkigt and Stadler (1986, as cited in Balmer, 2001) suggest four elements of corporate identity: *personality*, *behaviour*, *communication* and *symbolism*, while van Rekom (1997) identifies three elements: essence features of the firm, features that set it apart from others and continuity of the features over time. According to Balmer and Soenen (1999), corporate identity encompasses three elements: the ‘*mind*’ (the expressed organisational ethos, vision, strategy and product performance), the ‘*soul*’ (distinctive corporate values of the firm) and the ‘*voice*’ (the various ways of communicating to key stakeholder groups). In short, corporate identity is the bonding of strategy, structure, communication and culture, embracing both tangible (e.g. name, logo, colour) and intangible (e.g. firm’s behaviour and reputation) elements that make it distinctive (Balmer, 2001, p. 280).

Balmer and Soenen (1999) further operationalised four distinctive features of corporate identity using the mnemonic ‘ACID’, each letter representing a distinct identity type: *actual*, *communicated*, *ideal* and *desired*. *Actual identity* encompasses the business strategy, values and philosophy, corporate culture and structure (Gray and Balmer, 1998) while *communicated identity* is closely linked to image and reputation, which in turn leads to the realisation of *desired* (what corporate management wants it to be) and *ideal* identities (what stakeholders see as optimal). Since there exists an explicit covenant or ‘a promise’ (Johansson and Hirano, 1999; Mitchell, 1999) between an organisation and its key stakeholders, corporate identity must be managed so as to ensure alignment between the various identities suggested by Balmer and Soenen (1999). This entails communicating and behaving in a manner that leaves a pleasant impression with key stakeholders (Cornelissen and Elving, 2003).

One of the avenues through which information about corporate identity (e.g. its ideology, manage-

ment philosophy, products, commitments to society, etc.) is communicated is the corporate annual report. Hence, managing information disclosure in corporate annual reports in a consistent and pleasing manner will produce a positive corporate image and over time will produce a positive corporate reputation (Alessandri, 2001). In other words, through proper ‘communication management’, companies can build their reputation, which may lead to competitive advantage (see the operational model for managing corporate identity by Gray and Balmer, 1998) and will pay off in both operational and financial ways (Dowling, 2001), as well as ensure business survival (Balmer and Stotvig, 1997; van Riel and Balmer, 1997).

Islamic banks are representative of a new wave of corporations whose social goals are at least (if not more) as important as making profit. Based on the definition by Gray and Balmer (2001), such corporations fit what they described as having ‘ethical identity’. They studied two such corporations – Migros and Patagonia – to find commonalities that exist between them. Berrone et al. (2005) assessed the impact of corporate ethical identity on the firm’s financial performance and their results indicate that ‘revealed ethics’ (aspects of communication of the ethical identity) have informational worth and enhance shareholder value, while ‘applied ethics’ (all actions and policies considered as ethical and beyond communication of ethical values) have a positive impact through the improvement of stakeholder satisfaction. Since commonalities already exist between Islamic banks, as they are based on the Islamic ethical business framework drawn from the *Shari’ah* (Islamic law, often referred to as ‘ethics in action’), it would be interesting to assess whether an ‘ethical-identity gap’ exists and its implications on corporate branding and corporate image and reputation.

Hence, in this article, we attempt to assess the degree of variation of *communicated* ethical identity (as disclosed in the corporate annual report) against a benchmark of *ideal* ethical identity (checklist constructed based on Islamic precepts) for the Islamic banking sector where trust is vital.<sup>1</sup> Specifically, we measure the degree of ethical identity of seven Islamic banks in the Arabian Gulf region based on their corporate annual reports for the years 2002–2004 inclusive, using what we term an *Ethical Identity Index (EII)*. The reason for confining our scope to Islamic

banks in the Arabian Gulf region is because these countries share a similar socio-economic structure, which as such enables us to control for macro and cultural effects and make comparison and interpretations more meaningful. We chose corporate annual reports rather than other media of communication<sup>2</sup> in assessing *communicated* ethical identity because they offer a snapshot of management's mindset in a particular period (Neimark, 1992), have greater potential to influence due to widespread distribution (Adams and Harte, 1998), are more accessible for research purposes and are used by a number of stakeholders as the sole source of certain corporate information (Deegan and Rankin, 1997). The results of our survey, analysis and discussion constitute a further contribution to corporate identity, corporate communication, corporate social responsibility and Islamic banking literature.

The article proceeds as follows. The next section presents a literature review on various aspects of Islamic banking and discusses what constitutes the *ideal* ethical identity based on the Islamic precepts. The third section describes the research method. The fourth section presents our results and discussion, followed by the conclusions, implications and avenues for further research in the final section.

## Review of literature

Islamic banking received substantial attention following the Islamic resurgence in the 1970s and the increasing concern regarding the relationship between religion and economic activities among Muslims. There are now more than 200 Islamic financial institutions operating in 23 countries with more than US\$200 billion in deposits, and bankers estimate that the market is growing by at least 15% a year (International Herald Tribune, 2003). Despite growing acceptance of Islamic banking, there is still scepticism on the 'purity' of the products offered and also the 'sincerity' of those managing the institutions. Others mention that one of the basic problems with Islamic banking is that "*Homo Islamicus* [Islamic man] keeps acting a lot like *Homo economicus* [economic man]" (Useem, 2005). On the one hand, Islamic banks are perceived as being too complacent, believing they have a captive market in the Muslim masses who will come to them on religious grounds

alone, and in the process lose non-Muslim potential customers interested in investing in organisations whose activities are regarded as ethical. On the other hand, they have been criticised as being so anxious to tap funds from the Muslim masses that they opt for pragmatism over purity in the products offered, and in the process destroy the confidence of their Muslim customers. In short, Islamic banks as value-oriented organisations need to assess their corporate ethical identity and corporate branding process, as their current state seems to be controversial. Since we are not aware of any studies that specifically attempt to assess the strength of Islamic banks' *communicated* ethical identity against a benchmark of *ideal* ethical identity, a discussion of what constitutes the *ideal* ethical identity based on the Islamic precepts follows.

### *The ideal ethical identity benchmark*

Islamic banking refers to a system of banking which is consistent with the principles of Islamic law (*Shari'ah Islami'iah*). The *Shari'ah* governs every aspect of a Muslim's life, viz. spiritual, economic, political and social, and faithful execution of duties and obligations based on the *Shari'ah* is recognised as a form of worship. The *Shari'ah* is concerned with promoting justice and welfare in society (*al-adl* and *al-ihsan*) and seeking God's blessings (*barakah*), with the ultimate aim of achieving success in this world and hereafter (*al-falah*).

There are five distinctive features that differentiate Islamic Banks (IBs) from their competitors (conventional banks): (a) underlying philosophy and values; (b) provision of interest-free products and services<sup>3</sup>; (c) restriction to Islamically acceptable deals; (d) focus on developmental and social goals; and (e) subjection to additional reviews by the *Shari'ah* Supervisory Board (SSB). Hence, Islamic banks, as economic and social institutions, must portray aspects of those five traits, drawn from both *Shari'ah* and business ethics,<sup>4</sup> in their activities. These features form the *ideal* ethical identity benchmark used in this study, which is further described in the following paragraphs.

### *The underlying philosophy and values*

As mobilisers of savings on a large scale and caterers to fund-seekers in all sectors of the economy, IBs

play an important role in economic regeneration and social justice (Siddiqi, 1995). They have been entrusted with the safekeeping of depositors' savings and shareholders' capital and putting these funds to good use. Hence, they are not only financially accountable but also morally accountable for their business behaviour. As such, we expect IBs to communicate clearly the following in their annual reports:

- (i) commitments to operate within *Shari'ah* principles/ideals;
- (ii) commitments to provide returns within *Shari'ah* principles/ideals;
- (iii) commitments to engage in investment activities that comply with *Shari'ah* principles;
- (iv) commitments to engage in financing activities that comply with *Shari'ah* principles;
- (v) commitments to fulfil contractual relationships with various stakeholders via 'contract (*uqud*) statements';
- (vi) current and future directions in serving the needs of Muslim communities;
- (vii) statements of appreciation to stakeholders.

Current and prospective shareholders and fund depositors would ideally like to assess and judge the credentials of those who have been entrusted with their funds and who have full authority in making economic decisions on their behalf in enforcing the rules of God. In other words, those who manage and govern IBs are expected to be believers imbued with piety and righteousness, and to have knowledge and competence in relevant fields associated with banking as well as knowledge of *Shari'ah*, especially those areas related to business transactions (*fiqh al-mu'amalat*). Hence, we expect IBs to communicate the following aspects of management to their stakeholders:

- (i) names, positions and pictures of board members and top management;
- (ii) profile of board members and top management as indicators of their knowledge of and competence in banking and *Shari'ah*;
- (iii) aspects of good corporate governance: balanced board, no role duality, having an audit committee, limited multiple directorships and shareholdings.

#### *Provision of interest-free products and services*

Unlike the foundation of conventional banking, which is interest based (*riba*), IBs must avoid any form of such dealings, as Islam strongly prohibits interest, as found in four different revelations in the *Qur'an*.<sup>5</sup> Consequently, the various financial instruments developed by IBs have been based on two principles: the profit-and-loss sharing principle and the mark-up principle (Aggarwal and Yousef, 2000). Financing instruments based on the former principle include *mudharabah* (venture capital) and *musharakah* (partnership arrangement), while instruments based on the latter include *murabahah* (resale with stated profit), *bay'al-salam* (forward sale contract), *ijarah* and *ijarah wa iqtina* (operating and financial lease). To remain competitive, IBs have been innovative in their offering of products that do not violate *Shari'ah* but to a certain extent, they are still perceived as 'Islamising' products and instruments of the capitalistic system rather than applying their own minds in developing products based on Islamic concepts. With fierce competition, more sophisticated markets and demand for more transparency by stakeholders, one of the ways in which IBs can deal with those matters is to communicate effectively regarding the following:

- (i) details of investment activities;
- (ii) if new products have been introduced, whether they have been approved by the SSB (*ex-ante*) as well as an explanation of the basis of the *Shari'ah* concept legitimising the new product.

#### *Islamically acceptable deals*

Islamic banking is much more than offering interest-free products. IBs should only finance projects or support practices and products that are permissible (*halal*) and avoid financing or investing in activities considered abhorrent in Islam, such as gambling, alcohol, drugs, etc., or in short, those that bring harm to society and the environment. IBs must also avoid speculative transactions or excessive risks (*gharar*), such as investments in futures markets, since the consequence is not known. In Islam, parties to the contract should have perfect knowledge of the counter values intended to be exchanged and cannot predetermine a guaranteed profit. The rationale



behind the prohibition is the wish to protect the weak from exploitation and as such goes beyond financial accountability to include accountability to society. Hence, IBs should communicate in their annual reports the following:

- (i) any involvement in non-permissible activities;
- (ii) if involved in non-permissible activities, the reason for involvement, the percentage of profit from such activities and how gains from such activities have been handled.

#### *Focus on developmental and social goals*

IBs are expected to be more socially responsible than their conventional counterparts, as Islam emphasises social justice. One of the indicators is their contribution to and management of *zakah* (religious levy), *saddaqa* (charity) and *qard-hassan* (benevolent loans) funds. *Zakah* is one of the five pillars of the Islamic faith and the spending of the proceeds and the beneficiaries<sup>6</sup> are specified in the *Qur'an*. They are God's laws and non-fulfilment is a sin and will result in punishment in the hereafter. However, there have been mixed opinions as to which party is liable for *zakah*: banks or individuals (i.e. shareholders and depositors). Regardless of who is liable, what is more important is for the IB to communicate the following details:

- (i) which party is liable for *zakah*;
- (ii) if the bank is liable, whether *zakah* has been paid, the sources of *zakah* funds, the uses of the *zakah* funds,<sup>7</sup> any balance of *zakah* not distributed and the reason for it, and attestation from the SSB that they have been properly computed and that the sources and uses of the funds are legitimate based on God's rules.

Unlike *zakah*, which is obligatory, *saddaqa* (charity) is voluntary in nature and can be used for purposes allowed by *Shari'ah* for the benefit of society. Hence, IBs should communicate:

- (i) the amount and the sources and uses of charity funds, separate from the *zakah* funds.

Providing *qard-hassan* (benevolent or interest-free loans) for socially beneficial causes is an important social contribution that IBs may make, especially to

the local community in which they operate. As such, IBs should ideally communicate the following in their annual reports:

- (i) the amount and the sources and uses of such funds;
- (ii) the banks' policies in providing such funds and how non-repayment of such funds will be dealt with.

Other revealing indicators of an organisation's ethical stand from an Islamic perspective are the ways it treats its employees and debtors as well as its commitments to society. Employees are the greatest asset of the business and their welfare should be given due attention. It is the responsibility of employers to ensure that employees are paid fair wages,<sup>8</sup> not overworked<sup>9</sup> and have the opportunity to fulfil their spiritual obligations. Equal opportunity is also stressed in Islam.<sup>10</sup> For IBs to be successful in a highly competitive services sector, there must be consistency between the brand values and staff behaviour. In other words, an adequate supply of capable, trained personnel with knowledge and understanding of the principles underlying Islamic banking and a strong belief in it is one of the ingredients for success, echoing de Chernatony and Segal-Horn (2001), who mentioned that a successful services brand is dependent on genuine staff conviction and commitment. Hence, the following should be communicated in the annual report:

- (i) employees' welfare;
- (ii) training and development (especially on *Shari'ah* awareness), amount spent on training, provision of special training or recruitment schemes;
- (iii) equal opportunity;
- (iv) reward to employees.

Debtors receive special attention in Islam. Lenders are asked to be lenient with their debtors and in certain circumstances, debtors are entitled to receive *zakah* and debts should be written off as charity.<sup>11</sup> As such, IBs are expected to demonstrate and communicate such commitments in their annual reports:

- (i) debt policy and type of debt;
- (ii) amount of debts written off.

Public duties in Islam are seen as a part of the general meritorious and ethical tendency of the faith (Dien, 1992). The circumstantial needs of the community within which the IBs operate should first be catered to. Hence, IBs should ideally communicate the following to indicate their commitments to society:

- (i) having a female branch (since our focus is on those IBs in the Arabian Gulf region);
- (ii) creating job opportunities;
- (iii) supporting organisations that benefit society and participating in government social activities;
- (iv) sponsoring Islamic educational and social events.

#### *Reviews by the Shari'ah Supervisory Board (SSB)*

All Islamic banks have a *Shari'ah* Supervisory Board (SSB) whose role is to ensure that any new formulations and modalities are in line with *Shari'ah* principles and within the ambit of Islamic norms. In other words, the SSB acts as an internal control mechanism and its primary objective is '... to give credibility to the operations of Islamic banks by authenticating their legitimacy from the *Shari'ah* point-of view' (Mudawi, 1984, p. 4). Membership of SSBs is often drawn from the professional specialist of Islamic jurisprudence (*u'lama*) (Gambling et al., 1993) and they perform all or part of the following duties: setting the *Shari'ah* rules for the conduct of banking business; examining all or part of the bank's transactions to ascertain whether there have been breaches of the *Shari'ah* rules; and issuing a statement in the annual report of the bank as to whether or not the bank has conducted its business in compliance with the *Shari'ah* (Karim, 1990). Confidence in the *Shari'ah* scholars is the bedrock of Islamic banking and any doubts concerning their integrity and ability to handle complex financial systems and keep the operation Islam compliant may lead to a loss of confidence in the system. Thus, the SSB report should ideally communicate:

- (i) names, pictures and remuneration of SSB members;
- (ii) number of meetings held;
- (iii) whether there are defects in the products offered and if there are, what are their recom-

mendations to rectify the defects and the actions taken by management;

- (iv) basis of examination of the documents;
- (v) attestation that profits are gained lawfully;
- (vi) signatures of all members.

In short, communication of the detailed aspects of the five traits described above would help annual report users gauge the *ethical* identity of IBs. However, as mentioned by Fukukawa and Moon (2004), one common problem in communication management is deciding the extent and format of disclosure, because communication does not necessarily denote activity and its absence does not necessarily indicate non-activity. The communication decision gets more complicated when ethics is the basis for deciding the 'rights' and 'responsibilities' of users and providers of corporate information, respectively, due to the absence of a certain *communis opinio* (common opinion) on human ethical or moral reasoning, which thus increases conflicts of interest between different groups in society (Haniffa and Hudaib, 2002). In addition, as argued by Gray et al. (1996), 'rights' and 'responsibilities' based on ethics could be 'absolute' (unvarying with time and place) or 'relative' (changing with time and place), depending on one's interpretation. But for Muslims, the *Shari'ah* is considered as both 'stable' (based on the *Qur'an* and *Hadith*, i.e. sayings, approvals and actions of the Prophet Muhammad) and 'dynamic' (based on *Ijma'*, i.e. consensus of Muslim scholars, and *Qiyas*, i.e. represented in the analogical deductions from the other three sources for contemporary issues that are not directly mentioned in those sources but have similar characteristics to those that existed in the past) and it addresses the *oeconomicus*, *eticus* and *religiosus* needs of their stakeholders. In other words, IBs are perceived as institutions enabling their stakeholders to fulfil their economic needs with assurance that they are within the dictates of their religious faith and business ethics. In short, Islam encourages economic endeavours and the maximisation of profit, but this must be within the bounds of the religion and business ethics.

Having identified the dimensions of the *ideal* ethical identity for IBs, the next stage is to assess whether disparities exist between the *communicated* and *ideal* ethical identities. The following section describes our research method.

## Research method

The population of our study consists of IBs operating in the Arabian Gulf region, which encompasses Bahrain, Saudi Arabia, Qatar, Kuwait, Oman and the United Arab Emirates. Our sample was initially based on the list of Islamic financial institutions on the website IBF NET (<http://www.Islamic-finance.net/bank.html>). There are 24 such institutions in the region (including investment banks and insurance providers) and our final sample consists of seven Islamic banks in four of those countries<sup>12</sup> whose annual reports for the years 2002–2004 were available in an English version on the Internet. These banks are Abu Dhabi Islamic Bank (ADIB), Al-Baraka Bank (ABB), Al-Rajhi Bank (ARB), Bahrain Islamic Bank (BIB), Dubai Islamic Bank (DIB), Kuwait Finance House (KFH) and Shamil Islamic Bank (SIB).

To explore the communication practices of IBs in our sample, we used content analysis, which is a method of codifying the text (or content) of a piece of writing into various groups (or categories) depending on selected criteria (Krippendorff, 1980; Weber, 1988). An essential element of content analysis is the selection and development of categories into which content units can be classified. The categories and items were drawn mainly from our understanding of Islamic literature as discussed in the last section and the Islamic perspective of a social responsibility reporting framework suggested by Haniffa (2002). We also considered items required to be disclosed by the Accounting and Auditing Organisation for Islamic Financial Institutions (AAOIFI, 2001) and previous research in the area of social responsibility reporting (Cowen et al., 1987; Ernst and Ernst, 1978; Gray et al., 1995; Guthrie and Parker, 1989, 1990).

Since the interest is to assess the degree of congruence between the *ideal* and *communicated* ethical identities, we designed our research instrument (checklist) to cover aspects of the five traits (themes) constituting the *ideal* ethical identity as suggested in the last section. The five themes were extended into eight dimensions. The first theme, 'underlying philosophy and values', consists of two dimensions: vision and mission of the organisation and details of its board of directors and top management, including aspects of good corporate governance practice. The second and third themes, viz. 'interest-free product' and 'engagement in only Islamically acceptable deals

(*halal*)', are both addressed under the dimension products. Aspects of the fourth theme, 'focus on developmental and social goals', are covered under four dimensions: *zakah*, charity and benevolent loans; employees; debtors; and community. The fifth theme, 'additional reviews by the *Shari'ah* Supervisory Board', is addressed under the dimension SSB. We further identified constructs under each dimension based on prior literature including those that capture pictures and graphics, as they are powerful and highly effective methods of communication (Beattie and Jones, 1992, 1994; Preston et al., 1996) and excluding them may be considered a limitation. The final *ideal* ethical identity checklist instrument consists of 5 themes, 8 dimensions and 78 constructs (see Appendix).

Two methodological issues related to content analysis are reliability and validity (Weber, 1985). Reliability problems may arise due to ambiguity of meanings or category definitions while validity problems are related to the "extent to which (a variable) measures the construct the investigator intends it to measure" (Weber, 1985, p. 15). Hence, precautionary measures have been taken to improve both reliability and validity. One way of improving reliability is to use multiple coders (Holsti, 1969) and in this study, two coders scored the research instrument and any problems and discrepancies that arose were discussed and resolved accordingly via a set of basic coding rules. To enhance validity, categories were carefully developed from the extant Islamic and social responsibility literature.

The approach to scoring items is essentially dichotomous in that an item in the research instrument scores one if communicated and zero if it is not (see Haniffa and Cooke, 2002), although no penalty is imposed if the item is considered irrelevant.<sup>13</sup> To ensure that judgement of relevance is not biased, the entire annual report is read before any decision is made (Cooke, 1996). The approach to scoring is additive and equally weighted.<sup>14</sup> To assess the *communicated* and *ideal* ethical identities, we then expressed the scores in the form of an index, which we termed *Ethical Identity Index (EII)*, as follows:

$$EII_j = \frac{\sum_{i=1}^{n_j} X_{ij}}{n_j}$$



where  $EII_j$  is the ethical identity index,  $n_j$  the number of constructs or items disclosed by  $j$ th firm,  $n_j \leq 78$ , and  $X_{ij} = 1$  if  $i$ th construct or item is disclosed, 0 if  $i$ th construct or item is not disclosed, so that  $0 \leq I_j \leq 1$ .

We then ranked each bank based on their Ethical Identity Index ( $EII$ ). The higher the  $EII$ , the less the variation between the corporation's *communicated* and *ideal* ethical identities. In other words, a high  $EII$  suggests that the corporation has adopted a communication strategy that fits its religious ethical identity while a low  $EII$  suggests the need to improve its communication strategy to enhance its ethical image and reputation and to gain competitive advantage.

### Analysis and discussion of results

Table I presents the results of the overall  $EII$  and the ranking for the seven IBs for each of the 3 years examined in this study as well as the 3-year mean  $EII$  and ranking (see the bottom three rows of the table).

It can be seen from the table that the highest overall *Ethical Identity Index* ( $EII$ ) for three consecutive years goes to Bahrain Islamic Bank (BIB), followed by Shamil Islamic Bank (SIB), while the lowest  $EII$  for three consecutive years goes to Al-Rajhi Bank (ARB). In 2002, the  $EII$  ranged from 0.21 to 0.72, while in 2003 and 2004, the ranges were 0.12–0.63 and 0.14–0.61, respectively. The results suggest variation and inconsistencies between the *communicated* and *ideal* ethical identities over the 3-year period examined.

Based on the 3-year mean  $EII$  for each bank, it can be seen that the range was 0.16–0.65. This means that BIB had 65% of the constructs under the eight dimensions in the *ideal* ethical identity research instrument being communicated in their annual reports while ARB addressed only 16% of the constructs in the research instrument. In other words, the overall 3-year mean  $EII$  of 0.65 for BIB suggests that there is less discrepancy between the *ideal* and *communicated* ethical identities while the overall 3-year mean  $EII$  of 0.16 for ARB suggests a large disparity between the *ideal* and *communicated* ethical identities. As such, ARB may need to reassess its communication strategy to enhance the strength

of its ethical image and reputation in order to stay competitive.

Table I also shows the  $EII$ , ranking and the 3-year mean  $EII$  under each dimension (see rows 1–8). The last four columns of the table show the annual mean  $EII$  under each dimension and the overall mean  $EII$  and ranking based on 21 observations for each dimension. This is further discussed below.

#### *Dimension: vision and mission statement*

Under the dimension 'vision and mission', BIB scored the highest  $EII$ , followed by ADIB, with DIB being the lowest for three consecutive years. The  $EII$  for this dimension seems to improve over the 3-year period for three banks, BIB, DIB and KFH; is constant for ABB and ARB; and fluctuates in the case of ADIB and SIB. The 3-year mean  $EII$  for this dimension (based on each bank) ranged from 0.04 to 0.85. We noted that DIB did not communicate any constructs under this dimension in 2002 and 2003 but did so in 2004, while BIB communicated all constructs under this dimension in 2004.

One possible explanation for DIB addressing this dimension in 2004 is due to a desire to increase its competitiveness in the region, as suggested in its annual report:

*Undoubtedly, these accomplishments pose further challenges to the Bank in its endeavour to maintain and accelerate its growth. Thus, during 2005 and the years to come, the Bank endeavours to expand its activities and widen its operations to cover regional markets by opening new branches or representative offices; by concluding new strategic alliances and partnerships with major local and international companies and by launching specialized and diversified investment portfolios with an aim to enhance shareholders' value (DIB Annual Report 2004, p. 2).*

Similarly, a desire to increase its competitiveness in the region seems to have caused BIB to enhance its communication strategy in 2004, as evidenced in the following statement:

*With a strong and growing network of branches, currently numbered at 12, the Bank is well positioned to meet strong and growing demand in the market for banking, financing and investment opportunities on behalf of individuals and*

TABLE I  
Annual ethical identity index and ranking under each dimension across IBs

	ADIB				ABB				ARB				BIB				DIB				KFH				SIB				Annual Mean EII for each Dimension				Overall mean (rank)		
	EII (rank)		EII (rank)		EII (rank)		EII (rank)		EII (rank)		EII (rank)		EII (rank)		EII (rank)		EII (rank)		EII (rank)		EII (rank)		EII (rank)		EII (rank)		EII (rank)		EII (rank)						
	2002	2003	2004	2005	2002	2003	2004	2005	2002	2003	2004	2005	2002	2003	2004	2005	2002	2003	2004	2005	2002	2003	2004	2005	2002	2003	2004	2005	2002	2003	2004	2005			
1) Vision & Mission statements	0.44 (2)	0.66 (2)	0.33 (2)	0.33 (2)	0.33 (3)	0.33 (4)	0.33 (2)	0.33 (2)	0.11 (6)	0.11 (6)	0.11 (6)	0.11 (6)	0.77 (1)	0.77 (1)	1.00 (1)	0.11 (6)	0 (7)	0 (7)	0.11 (6)	0.22 (5)	0.33 (4)	0.33 (2)	0.33 (3)	0.44 (3)	0.31	0.38	0.33 (2)	0.36	0.35 (7)						
	0.48*				0.33				0.11				0.85				0.				0.				29				0.37						
2) BODs and top management	0.08 (7)	0.15 (6)	0 (7)	0 (7)	0.31 (4)	0.62 (2)	0.62 (2)	0.62 (2)	0.15 (6)	0.15 (6)	0.08 (6)	0.08 (6)	0.69 (1)	0.46 (4)	0.54 (3)	0.23 (5)	0.23 (5)	0.23 (5)	0.23 (5)	0.54 (3)	0.54 (3)	0.54 (3)	0.54 (3)	0.62 (2)	0.69 (1)	0.37	0.41	0.69 (1)	0.39	0.39 (5)					
	0.08				0.52				0.13				0.56				0.				23				0.				54				0.67		
3) Product & services	0.50 (5)	0.40 (3)	0.40 (3)	0.40 (3)	0. (7)	0.25 (5)	0.25 (6)	0.25 (6)	0.30 (6)	0.13 (6)	0.13 (7)	0.13 (7)	0.86 (1)	0.86 (1)	0.71 (2)	0.80 (2)	0.80 (2)	0.80 (2)	0.60 (4)	0.60 (4)	0.60 (4)	0.40 (3)	0.71 (3)	0.30 (4)	0.54	0.41	0.41	0.54	0.47(2)						
	0.43				0.17				0.19				0.81				0.				84				0.				38				0.44		
4) Zakah, charity & benevolent loans	0.38 (3)	0.38 (3)	0.38 (3)	0.38 (3)	0.50 (2)	0.50 (2)	0.50 (2)	0.50 (2)	0.27 (5)	0.20 (7)	0.20 (7)	0.20 (7)	0.67 (1)	0.80 (1)	0.80 (1)	0.15 (7)	0.23 (6)	0.31 (5)	0.36 (4)	0.36 (4)	0.36 (4)	0.36 (4)	0.25 (6)	0.25 (6)	0.37	0.39	0.25 (6)	0.40	0.39 (5)						
	0.38				0.50				0.22				0.76				0.				23				0.				36				0.25		
5) Commitments toward employees	0.67 (1)	0.56 (2)	0.44 (2)	0.44 (2)	0.33 (4)	0.22 (5)	0.22 (6)	0.22 (6)	0.33 (4)	0.10 (7)	0.10 (7)	0.10 (7)	0.67 (1)	0.44 (4)	0.44 (2)	0.10 (7)	0.22 (5)	0.33 (4)	0.33 (4)	0.33 (4)	0.33 (4)	0.56 (2)	0.56 (3)	0.78 (1)	0.43	0.41	0.67 (1)	0.36	0.40 (4)						
	0.56				0.25				0.18				0.52				0.				22				0.				41				0.67		
6) Commitments toward debtors	0.67 (4)	0.33 (5)	0.33 (5)	0.33 (5)	0.67 (4)	0.67 (3)	0.67 (3)	0.67 (3)	0.33 (7)	0.33 (5)	0.33 (5)	0.33 (5)	1.0 (1)	1.0 (1)	1.0 (1)	1.0 (1)	1.0 (1)	1.0 (1)	1.0 (1)	1.0 (1)	1.0 (1)	0.67 (4)	0.67 (4)	0.33 (5)	0.76	0.67	0.62	0.68 (1)							
	0.44				0.				0.33				1.0				1.0				0.80				0.44				0.44						
7) Commitments toward society	0.29 (1)	0.29 (3)	0 (6)	0 (6)	0.14 (4)	0.14 (4)	0.14 (2)	0.14 (2)	0.14 (4)	0 (7)	0 (6)	0 (6)	0.29 (1)	0.14 (4)	0.14 (2)	0 (7)	0.14 (4)	0.14 (2)	0.29 (1)	0.29 (1)	0.29 (1)	0.14 (4)	0.43 (2)	0.14 (2)	0.18	0.24	0.12	0.18 (6)							
	0.19				0.14				0.05				0.19				0.				0.				38				0.24						
8) SSB	0.50 (4)	0.50 (4)	0.50 (4)	0.50 (4)	0.60 (3)	0.70 (1)	0.70 (1)	0.70 (1)	0.10 (7)	0 (7)	0.25 (7)	0.25 (7)	1.0 (1)	0.67 (2)	0.54 (3)	0.30 (5)	0.40 (5)	0.40 (5)	0.27 (6)	0.27 (6)	0.27 (6)	0.27 (6)	0.63 (2)	0.63 (3)	0.49	0.45	0.63 (2)	0.47 (2)							
	0.50				0.67				0.12				0.74				0.				37				0.				0.63						
Overall EII	0.41	0.41	0.29	0.43	0.34	0.43	0.43	0.43	0.21	0.12	0.14	0.14	0.72	0.63	0.61	0.22	0.28	0.33	0.41	0.42	0.38	0.48	0.51	0.48	0.45	0.47	0.47 (2)								
Overall rank:	3	5	6	3	5	3	3	3	7	7	7	7	1	1	1	6	6	5	3	4	4	2	2	2	2	2	2	2							
3-year mean EII:	0.37 (5)			0.40 (3)					0.16 (7)				0.65 (1)			0.28 (6)				0.40 (3)			0.48 (2)												

Note: \* Refers to three-year mean *EII* for each bank under each dimension.

*institutions with the highest ethical standards and an unwavering commitment to the principles of Islamic Shari'ah* (BIB Annual Report 2004, p. 2).

Unlike other IBs that tend to emphasise commitments to operate within *Shari'ah* principles, ARB and DIB did not clearly state this in their annual reports for all 3 years examined. This sends two signals: either management knows that its operations are not truly Islamic and wants to play down that image or simply management do not foresee the need to do so as their reputation as an IB is well established (given that DIB and ARB were incorporated as IBs in 1975 and 1987, respectively). Interestingly, despite being incorporated as an IB in 1979, BIB continues to consistently emphasise this aspect.

Four IBs (except KFH, DIB and ARB) stated one of their objectives to be maximising shareholders' return or value but none used stronger words concerning the assurances and commitments expected of an IB, such as 'maximum *halal* (legitimate) returns' or 'returns from *halal* (legitimate) sources' rather than simply 'maximising returns.' The use of the latter phrase does not help in differentiating between the goals of an IB and those of conventional banks.

In terms of current and future directions in serving the needs of the Muslim community and society, BIB consistently stated its commitment to this aspect. For instance, it stated in its annual report:

*... contribute towards the development of an Islamic economic model and play an important role in local events and charitable causes* (BIB Annual Report 2002, p. 3).

#### *Dimension: BODs and top management*

With regard to the dimension 'board of directors', the *EII* of only DIB and KFH seemed to be consistent for all 3 years. BIB reduced communication (removing pictures of board members and management and information regarding shareholdings) in 2003, while ADIB, ABB and SIB increased communication, especially regarding top management. In 2004, ADIB and ARB reduced their communication while BIB increased theirs. The inconsistent communication over the 3-year period regarding this aspect is a bit puzzling and we cannot find any specific corporate characteristics, for instance prof-

itability or diversification, nor any significant events or corporate culture characteristics that may have caused this anomaly.

The 3-year mean *EII* for the seven banks under this dimension ranged from 0.08 to 0.67, the lowest being ADIB and the highest, SIB. The principal-agent relationship means entrusting the agent with resources to be put to good use and holding the agent responsible for the conduct of the business. Accordingly, this trusteeship entails assessment of the profile of those conducting the business. Hence, credentials of those entrusted to conduct the business would enable users of annual reports to make their judgement. Unfortunately, none of the IBs communicate much on their board members and top management. From the results of the survey, it also seems that good corporate governance practice (as opposed to religious governance, which is the function of the SSB) is still lacking among IBs operating in this region. Hence, the boards and top management of the organisations, who shape, define and communicate their companies' identities to achieve corporate goals and ensure long-term survival (Topalian, 2003), need to consider communicating this aspect more consistently.

#### *Dimension: product and services*

The uniqueness of the IBs is related to the type of products and services that they offer, which has to be different from that offered by conventional banks. In the interest of shareholders and depositors as well as other stakeholders, IBs need to be transparent, to give full and accurate information about their products and services, and to keep interested parties well informed. Hence, corporate communication strategy on product-related information is important for users of corporate annual reports to assess and judge the IBs' ethical business conduct. We found BIB and DIB to have the highest *EII*, with the latter getting a full score in 2004 with regard to this dimension. We also found communication on this aspect dropped in 2003 for ADIB, ARB, KFH and SIB. Only DIB and KFH experienced an increase in *EII* for 2004. One possible explanation in the case of KFH is due to close monitoring by the central bank:

*By the Grace of God, KFH was able to apply the Kuwait Central Bank's Reports System that ensures fulfilling the Central Bank's requirements with respect to data and information consistency and compatibility that reflect the Bank's financial position and its customers' base as a part of its adherence to instructions regarding the Central Banks' controls in application of the Islamic Banks' Law No. 30 of 2003. This positively reflects the Islamic financial march, improves the performance efficiency, strengthens the Bank's local and international transparency, and strengthens Kuwait's progress as a major Islamic financial service provider (KFH Annual Report 2004, p. 10).*

The 3-year mean *EII* under this dimension ranged from 0.17 to 0.84, with the lowest for ABB and the highest for DIB. Only two IBs clearly stated no involvement in non-permissible activities. Three IBs disclosed that they have introduced new products and services for all 3 years while two others mentioned this once. Only two IBs clearly indicated that the new products had been approved by the SSB and further stated the basis of the *Shari'ah* concept for the new product, reinforcing the legitimacy of their new product:

*The Al Khair financing scheme... approved by the Bank's Shari'ah Board, which is patterned along the lines of the Shari'ah Tawaruk which has been approved by the Islamic Fiqh academy of Makkah Al Mukaramah... (ADIB Annual Report 2002, p. 7).*

Since most of the products offered by IBs are in Arabic terms, three IBs provided a glossary or a list of definitions of the products in the report to familiarise non-Arabic speakers to the products. All IBs disclosed details of their investment and financing activities. However, the financing activities of KFH as stated in the following statement raises concern on the legitimacy of its claim of adhering to Islamic principles when clearly there is a combination of conventional and Islamic financing:

*...participated in financing the purchase of an Airbus plane for Emirates Airlines in cooperation with international Islamic institutions... This deal combined conventional and Islamic financing, which is a concept pioneered by KFH in the Equate financing transaction. This represented a significant achievement for the Islamic banking industry (KFH Annual Report 2002, p. 17).*

Interestingly, KFH did not communicate details of their financing activities in 2003 but did so in 2004 with a different tone:

*The Company signed two leasing agreements. The first USD70 million leasing agreement is to buy two aircrafts in which the Bank's contribution amounted to USD35 million while the Bank's share amounted to USD35 million in the second USD98 leasing agreement to increase the Bank's business activities in this sector to USD500 million. The Bank issued (MALC) Fund for subscription last year whose assets are expected to reach USD600 million (KFH Annual Report 2004, p. 12).*

#### *Dimension: Zakah, charity and benevolent loans*

The highest *EII* under this dimension for three consecutive years goes to BIB, followed by ABB, ADIB and KFH. The lowest *EII* for 2002 was DIB and in 2003 and 2004, ARB. The lower level of communication by ARB in the latter years may be attributed to disputes regarding *zakah*. The 3-year mean *EII* ranged from 0.22 to 0.76, the lowest being ARB and the highest BIB.

For Muslims, payment of *zakah* is one of the acts of worshipping God. Besides *zakah*, God encourages man to spend their wealth on charity. Payment of *zakah* is not the responsibility of the IBs but that of the shareholders in Saudi Arabia, Kuwait and the United Arab Emirates, as stated below:

*... the management of the Bank is not authorized to pay Zakat directly, the responsibility of paying Zakat is that of the shareholders (ADIB Annual Report 2002, p. 10).*

Although *zakah* should be recognised as a religious levy rather than tax as understood in the current business world, ARB seems to treat *zakah* as a tax burden rather than a duty to fulfil one of the five pillars of the Islamic faith. The following statement indicates their underlying view on *zakah*:

*The Department of Zakat and Income (DZIT) issued zakat assessments for the years up-to 1998, which the Corporation appealed. The assessments and the zakat status for the years up-to 1990 has been finalized. The Corporation did not receive any assessments from the DZIT for the years after 1998. The Corporation's management believes that zakat provisions have been made for the expected zakat payments relating to prior years up to December 31, 2000 (ARB Annual Report 2002, p. 39).*



Such a statement indirectly supports the view of economic rationality where firms try to reduce their tax. If the true meaning of *zakah* is understood, there should not be disputes regarding the amount payable as any amount paid above the *zakah* threshold is considered charity. Interestingly, the same statement was communicated in 2004, suggesting that the dispute has still not been resolved.

Only BIB and DIB disclosed attestations from the SSB that the sources and uses of *zakah* and the amount computed for *zakah* was according to the Islamic principles. Although two IBs disclosed the balance on *zakah* and charity funds, neither provided reasons for the balance. Similarly, disclosure of sources and uses of charity was minimal except for KFH, especially in 2004, which may be related to the events in Iraq:

*To effectively serve the community, KFH took part in several development projects in and outside Kuwait.... Prisoners medical and orientation center was handed over by the contractor, which is built on 12,000 m<sup>2</sup> and accommodate 450 persons to have medical orientation programmes. KFH donated KD 1,425 million to the Ministry of Health to build new 15 aid centers to develop medical emergency services (KFH Annual Report 2004, p. 16).*

One unique feature of IBs is the provision of *qard al-hassan* (benevolent/good faith funds), i.e. providing loans without expecting any extra payment over and above repayment of the principal. Four IBs provide the statement of sources and uses of benevolent/good faith funds in their annual reports. However, some of the uses of such funds are questionable, especially when they are for extravagant purposes. The lack of policy as to who are eligible and the purpose of the funds may result in 'abuse' of such funds. The less advantaged in society should be given priority in accessing such funds if social justice is to be upheld by the IBs. In addition, the IBs should have a clear policy regarding non-repayment of such funds but this was not communicated by the IBs surveyed.

#### *Dimension: commitments toward employees*

The *EII* ranking for the seven IBs over the 3-year period was found to be inconsistent. In 2002, both ADIB and BIB shared the highest ranking but the position was taken over by SIB in 2003 and 2004.

DIB improved its position from being the lowest in 2002 to fourth in 2004. Based on the 3-year mean, SIB scored the highest followed by ADIB and BIB, with the lowest being ARB. The range for this dimension was from 0.18 to 0.67.

None of the IBs surveyed communicated on employees' welfare except for ARB in 2002, where they disclosed their commitments to provide medical benefits for their employees. However, in 2003 and 2004, SIB communicated more regarding employees' welfare:

*... a social committee was formed to organise social events involving employees and their families. A number of such events were organised which included a bowling competition, tennis tournament, football league, annual Ramadan dinner and long service awards for the employees as well as a boat trip to the Hawar Island. The Bank also organised a number of lectures by prominent scholars and specialist (SIB Annual Report 2003, p. 15).*

Four IBs indicated that they provide training for their staff to enhance their understanding of the *Shari'ah* related to Islamic banking transactions, as can be seen in the following statement by BIB:

*Staff was extensively educated about the Shari'ah aspects related to the Bank's business activities to enhance their understanding of Islamic banking transactions (BIB Annual Report 2002, p. 12).*

This effort is commendable because in offering unique products, it is vital that staffs are provided with special training to facilitate and improve the services offered. In other words, if employees are not well versed in the concepts of the Islamic banking system, they may not be able to serve or convince clients of the products offered, which may damage the corporate ethical identity.

#### *Dimension: commitments toward debtors*

The 3-year mean *EII* ranged from 0.33 to 1.0, the lowest being ARB and the highest position shared by BIB and DIB. Four IBs, viz. ADIB, ABB, ARB and SIB, did not communicate the amount of debts written off. In addition, both ADIB and SIB did not disclose their debt policy, while ARB was the only IB that did not provide details on type of lending

activities. In short, there is room for the IBs surveyed in this study to communicate more on this dimension.

*Dimension: commitments toward community and society*

The results indicate the KFH had the highest *EII* for three consecutive years with regard to this dimension. There was no communication on this aspect by DIB in 2002, by ADIB in 2004 and by ARB in 2003 and 2004. The general trend seems to be a decline in such communication for most of the IBs surveyed. The 3-year mean *EII* ranged from 0.05 to 0.38, the lowest being ARB and the highest KFH.

Despite corporate social responsibility forming an integral part of Islamic business ethics, it is surprising to find IBs not communicating much on this important aspect in their corporate annual reports. Three IBs indicated that they operate ladies' branches, as demonstrated in the following statement:

*... in support of the UAE businesswomen, the ladies branch...provides ladies with excellent banking services that combine traditional values with a progressive outlook (ADIB Annual Report 2002, p. 7).*

This indicates commitment to meeting societal values in a region where segregation of gender is common practice. In terms of commitments to social role, four IBs explicitly declared this. The following statements present disclosure by two of the IBs:

*... the Bank discharged its social responsibilities by donating good faith Qard fund for marriage, refurbishment, treatments, etc. (BIB Annual Report 2002, p. 37).*

*... through its participation in various community development programmes makes a sincere effort at making the society a better place to live in (ADIB Annual Report 2003, p. 18).*

Besides donating to charitable causes, one IB also indicated commitments to participate in government social activities, as disclosed in the following statement:

*In cooperation with the Kuwait Ministry of Health, KFH donated four million Kuwaiti Dinars to build a hospital for rehabilitation and treatment of drug addicts...participates in*

*the nation's fight against drug abuse and its negative social and economic effects on individuals and the society (KFH Annual Report 2002, p. 18).*

Sponsorship of events was communicated by only two IBs: ADIB in 2002 and SIB in 2003, as evidenced by the following statement:

*The Bank sponsored a number of conferences and exhibitions last year. These included the IMF-World Bank conference in Dubai, world economic forum in Jordan, world Islamic banking conference, the AAOIFI-World Bank conference and the MTC-Vodafone exhibition in Bahrain (SIB Annual Report 2003, p. 13).*

*Dimension: Shari'ah Supervisory Board (SSB)*

Under the dimension 'Shari'ah Supervisory Board', five IBs were found to communicate consistently over the 3-year period: KFH, ADIB, ARB, SIB and DIB. Interestingly, we observed a downward trend in communication on this aspect by BIB over the 3-year period. The 3-year mean *EII* also indicates three IBs to communicate more than 50% of the constructs under this dimension: ABB, SIB and BIB. Our observation suggests the driving force behind better communication on this aspect may be attributed to adoption of AAOIFI's ruling in Bahrain. ARB's *EII* is significantly lower (0.12) than the rest, indicating potential *communicated* ethical identity problems.

The SSB is entrusted with monitoring the conduct of those trusted with the resources (management) and providing assurance that the business is conducted according to the Islamic precepts. All IBs, with the exception of ARB, disclosed the names of their SSB members and only BIB disclosed the remuneration of their SSB members (in the notes to the account section of the annual report). Only BIB and SIB consistently indicated the number of meetings held.

In expressing an opinion on the operations of the IBs, the SSB report of BIB suggests that their reviews were based on all transactions, as indicated in the following extract from its annual report:

*The Shari'ah Supervisory Board's monitoring functions included the checking of the Bank's documents and procedures to scrutinize each single operation carried out by the*

*Bank, whether directly or through Shari'ah Internal Audit. We planned with Shari'ah Internal Audit Department to carry out monitoring functions through the acquisition of all information and clarifications that are deemed necessary to confirm that the Bank did not violate the principles and provisions of Islamic Shari'ah (BIB Annual Report 2004, p. 1, Section 2.)*

On the other hand, the SSB reports of ADIB, ABB and SIB clearly state that the reviews were based on samples. In terms of identifying whether there had been any defects in the transactions that they examined, the SSB of two IBs consistently reported no defects in the product, as in the following statement:

*... we certify confidently that all activities were practiced in compliance with Islamic Shari'ah and no violations have occurred, to the best of our knowledge (KFH Annual Report 2002, p. 9).*

The SSB reports of ADIB and ABB indicated defects and explained how they were rectified, as in the following statements:

*... management has been instructed to readdress defects found in some of such transactions and rectify their consequences (ADIB Annual Report 2002, p. 10).*

*Some transactions made by the Bank Branches in Pakistan where funds deposited with Islamic & Non-Islamic banks for investment in accordance with Shari'ah principles. We have noted partial irregularities in the operations of some of the said transactions where Shari'ah rules were not properly applied, accordingly part of the revenues were segregated (ABB Annual Report 2003, p. 5).*

The SSB report of ADIB further indicated that management has been directed to assign the profit earned through resources not in line with Islamic ethical principles to a charity account:

*Any profit earned through sources or methods that were not in line with sharia'a principles have been assigned to the charity account (Sadaqat) to be spent for charitable purposes as per our direction... (ADIB Annual Report 2002, p. 10).*

Surprisingly, despite the reporting of no defects in the transactions, there were conflicting statements in

the ABB's SSB report in 2002, as evidenced by the following:

*In our opinion the contracts, transactions and dealings entered into by the Bank...that we have reviewed are in compliance with the Islamic Shari'a Rules and Principles...*

*...all earnings that have been realized from sources or by means prohibited by Islamic Shari'a Rules and Principles have been disposed of to charitable causes (ABB Annual Report 2002, p. 15).*

The first statement emphasised compliance with Islamic teachings while the second statement suggests that some aspects of earnings were from illegitimate resources and that management had been advised to dispose them to charitable causes. Interestingly, in the following 2 years, the SSB reports of ABB clearly state the existence of defects and their recommendations to management, as in the following:

*We advised the Management to postpone dealings with parties not in compliance with Shari'a principles such cases like pre-determining profit rates and lack of proper documents. We have presented Islamic alternatives for similar cases and standard forms will be presented for approval by the Shari'a Board (ABB Annual Report 2003, p. 5).*

Only the SSB reports of DIB and ADIB consistently indicated that distribution of profits and losses were in line with Islamic teachings.

## Summary and concluding remarks

### *Overview of findings and implications*

Islamic Banks (IBs) exist to fulfil the financial (economic) needs of Muslims within the dictates of their religious faith. We extended the work of Gray and Balmer (2001) by attempting to measure the ethical identity of corporations that succeeded to form a niche market for themselves based on their ethical business philosophy. Since the foundation of the IBs' business philosophy is the *Shari'ah*, we are more interested in exploring their *communicated* ethical identity as opposed to *ideal* ethical identity. Specifically, we attempt to assess the strength or degree of ethical identity based on the variation between

the *communicated* and *ideal* ethical identities of such corporations. We developed a research instrument based on our understanding of the *Shari'ah* as well as the extant Islamic and corporate social responsibility literature to reflect the *ideal* ethical identity. Using content analysis, corporate annual reports for the period 2002–2004 of seven IBs in the Arabian Gulf region were scored based on the research instrument developed for the purpose. The results are expressed in the form of an index, which we termed the *Ethical Identity Index (EII)*: a high index indicates less variation and more inclination towards the *ideal* ethical identity while a low index suggests otherwise. The IBs surveyed were ranked based on the index under each dimension for each year.

Our survey results indicate the highest and lowest 3-year mean *EII* to be 0.65 (BIB) and 0.16 (ARB), respectively. This means that 65% of the constructs in our *ideal* ethical checklist have been communicated in the case of BIB and only 16% for ARB. The 3-year mean *EII* for the remaining five IBs ranged from 0.28 to 0.48, suggesting a large disparity between the *communicated* and *ideal* ethical identities. We also found the index of each bank to vary across the 3-year period, suggesting that communication is not static and often minimal. This may be attributed to a lack of pressure from and an indifferent attitude of stakeholders and also the prevailing secretive culture in the region. We further found the largest incongruence between the *communicated* and *ideal* ethical identities to be under four dimensions: commitments to society; their vision and mission; contribution and management of *zakah*, charity and benevolent loans; and information about top management. The findings are surprising because IBs, as social and economic institutions, are expected to communicate more on those dimensions to reflect accountability and justice not only to society, but also ultimately to God. Hence, managers of IBs may need to reflect on their communication management strategy as well as their image and reputation, not only from an ethical point of view but more importantly, from the perspective of religion. Good corporate communication and literature are vital for IBs to promote their corporate ethical identity. Unfortunately, some IBs put little effort into communicating their values in a consistent manner and

ensuring congruence between their rhetoric in the annual report and the ethical benchmark based on *Shari'ah*.

Our findings have important implications not only for managers of IBs in the region but also in other countries, such as Malaysia, Indonesia and Pakistan, where there is a large demand for Islamic banking products and services. Managers of IBs need to communicate more effectively and avoid ambiguous styles of communication, as these have important religious implications as well as implications for corporate image and reputation. Our findings also have important implications for academics and researchers in the area, as they pave the way for further investigation.

#### *Limitations and future research*

Our exploratory survey of communication in annual reports adds to prior related studies on corporate identity that have focused largely on the Western and capitalistic context and are less explicit concerning religion. However, the findings of this research are subject to several limitations. First, our study focused only on comparing the *communicated* and *ideal* ethical identities. Future research may want to consider comparing between (a) *actual* and *communicated* and (b) *actual* and *ideal* ethical identities. Such comparisons could provide evidence of the extent to which IBs engage in intentional distortions in their annual reports in efforts to enhance their ethical identities.

Second, our study focused only on communication in corporate annual reports even though it is known that management utilises other mass communication mechanisms. Hence, future research may consider disclosures in other media such as newspapers and in-house magazines. Since we restricted our sample to only IBs in the Arabian Gulf region, future studies can be extended to IBs in other countries as well as to conventional banks with Islamic windows.

Third, future research may consider other methodological approaches and also improve our research instrument. For instance, survey work involving more detailed interviews with management and stakeholders may help to enhance our understanding of the phenomenon.



## Appendix

## APPENDIX 1

## Research instrument used in the study

## Theme: underlying philosophy and values

*A. Dimension: vision and mission statement*

1. Commitments in operating within *Shari'ah* principles/ideals
2. Commitments in providing returns within *Shari'ah* principles
3. Focus on maximising shareholders returns
4. Current directions in serving the needs of Muslim community
5. Future directions in serving the needs of Muslim community
6. Commitments to engage only in permissible investment activities
7. Commitments to engage only in permissible financing activities
8. Commitments to fulfil contracts via 'contract (*uqud*) statement'
9. Appreciation to shareholders and customers

*B. Dimension: BOD and top management*

1. Names of board members
2. Positions of board members
3. Pictures of board members
4. Profile of board members
5. Shareholdings of board members
6. Multiple-directorships exist among board members
7. Membership of audit committees
8. Board composition: executive vs non-executive
9. Role duality: CEO is Chairman of board
10. Names of management team
11. Positions of management team
12. Pictures of management team
13. Profile of management team

## Theme: interest-free and Islamically acceptable deals

*C. Dimension: product*

1. No involvement in non-permissible activities
2. Involvement in non-permissible activities-% of profit
3. Reason for involvement in non-permissible activities
4. Handling of non-permissible activities
5. Introduced new product
6. Approval ex ante by SSB for new product
7. Basis of *Shari'ah* concept in approving new product
8. Glossary/definition of products
9. Investment activities-general
10. Financing projects-general

## Theme: Developmental and Social Goals

Appendix A1  
Contd.

## Theme: underlying philosophy and values

*D. Dimension: Zakah, charity and benevolent loans*

1. Bank liable for *zakah*
2. Amount paid for *zakah*
3. Sources of *zakah*
4. Uses/beneficiaries of *zakah*
5. Balance of *zakah* not distributed-amount
6. Reasons for balance of *zakah*
7. SSB attestation that sources and uses of *zakah* according to *Shari'ah*
8. SSB attestation that *zakah* has been computed according to *Shari'ah*
9. *Zakah* to be paid by individuals-amount
10. Sources of charity (*saddaqa*)
11. Uses of charity (*saddaqa*)
12. Sources of *qard al-hassan*
13. Uses of *qard al-hassan*
14. Policy for providing *qard al-hassan*
15. Policy on non-payment of *qard al-hassan*

*E. Dimension: employees*

1. Employees appreciation
2. Number of employees
3. Equal opportunities policy
4. Employees welfare
5. Training: *Shari'a* awareness
6. Training: other
7. Training: student/recruitment scheme
8. Training: monetary
9. Reward for employees

*F. Dimension: debtors*

1. Debt policy
2. Amount of debts written off
3. Type of lending activities-general
4. Type of lending activities-detailed

*G. Dimension: community*

1. Women branch
2. Creating job opportunities
3. Support for org. that provide benefits to society
4. Participation in govt. social activities
5. Sponsor community activities
6. Commitment to social role
7. Conferences on Islamic economics

Theme: Reviews by *Shari'ah* Supervisory Board*H. Dimension: Shari'ah Supervisory Board (SSB)*

1. Names of members
2. Pictures of members
3. Remuneration of members
4. Report signed by all members

Appendix A1  
Contd.

Theme: underlying philosophy and values

5. Number of meetings held
6. Examination of all business transactions ex ante and ex post
7. Examination of a sample of business transactions ex ante and ex post
8. Report defects in product: specific and detailed
9. Recommendation to rectify defects in product
10. Action taken by mgmt. to rectify defects in product
11. Distribution of profits and losses comply to *Shari'ah*

## Notes

<sup>1</sup> Another possibility of assessing the degree of variation in Islamic corporate identity is to compare between the *actual* and *communicated* ethical identities. However, we limited the scope of our research to only comparing between the *communicated* and *ideal* ethical identities because the comparison of *actual* and *communicated* ethical identities requires a different research methodology, such as symbolic interactionism using in-depth interviews.

<sup>2</sup> Internet communication is now becoming more popular for corporations to disseminate information regarding their achievements and goals, especially in terms of social responsibility. Fukukawa and Moon (2004) used website reporting to study communication of corporate social responsibility. We also looked at the Internet but concentrate only on the annual reports.

<sup>3</sup> Prohibition of interest or usury can also be found in the Old Testament (see Exodus 22:25, Leviticus 25:35–36, Deuteronomy 23:20, Psalms 15:5, Proverbs 28:8, Nehemiah 5:7 and Ezekiel 18:8, 13, 17 and 22:12).

<sup>4</sup> Sternberg (2000, p. 71), in discussing business ethics, differentiates between religious and non-religious ethical systems, arguing that the former focuses on the other world and is connected with the divine or the saving of souls and that its moral guidance for business is limited. For Muslims, the *Shari'ah* (Islamic teachings), which encompasses every aspect of life, does not draw distinctions between the two.

<sup>5</sup> The first revelation emphasizes that interest deprives wealth of God's blessings (Surah al-Rum, Chapter 30:39); the second condemns it as it is equivalent to wrongful appropriation of property belonging to others

(Surah al-Nisa, Chapter 39:161); the third revelation enjoins Muslims to stay clear of interest for the sake of their own welfare (Surah al-Imran, Chapter 3:130–132); and the fourth establishes a clear distinction between interest and trade, urging Muslims to take only the principal sum and to forgo even this sum if the borrower is unable to repay. It is further declared that those who disregard the prohibition of interest are at war with God and His Prophet. (Surah al-Baqarah, Chapter 2:275–281). See translation of The Holy *Qur'an* by Ali (1989).

<sup>6</sup> *Zakah* is a religious duty and type of worship levied on Muslim individuals only. The beneficiaries of *zakah* are the poor (*faqir*), the needy (*miskin*), the *zakah* collectors (*amil*), those who reconciled to Islam (*al-mua'lafah gulumabahum*), the captives and slaves (*riqab*), debtors (*gharim*), those serving the cause of God (*fi-sabilillah*) and the travellers (*ibn-al-sabil*). The rate is dependent on the type of economic activities (see El-Ashker, 1987, pp. 48–49).

<sup>7</sup> It is important for *zakah* recipients to know the source of *zakah*. If it is not of a lawful source, the recipients should abstain therefrom. In the modern world, it is the duty of the SSB, auditor and *zakah* officials to check the source of the *zakah* on behalf of the recipients.

<sup>8</sup> This aspect has been stressed in the *Hadith* (sayings of the Prophet Mohammad): as narrated by Abu Huraira: The Prophet said, "Allah said, 'I will be an opponent to three types of people on the Day of Resurrection: 1. one who makes a covenant in my name, but proves treacherous; 2. one who sells a free person and eats his price; and 3. one who employs a labourer and takes full work from him but does not pay him for his labour'" (Bukhari).

<sup>9</sup> This aspect is stressed in the following *Hadith*: "Do not tax the labourer with work which is beyond his powers" (Bukhari).

<sup>10</sup> This aspect is stressed in the *Hadith*: "He who has imposed, on a group of Muslims, a person who is inferior to another person who could be availed of, has behaved treacherously towards God, His Prophet, and the commonalty of Muslims" (Siddiqi, 1980).

<sup>11</sup> "If the debtor is in difficulty, grant him time till it is easy for him to repay. But if ye remit it by way of charity, that is best for you if ye only knew" (*Qur'an*, 2:280).

<sup>12</sup> We could not find annual reports for IBs in Qatar and our list did not indicate existence of any IBs in Oman.

<sup>13</sup> Some of the items in our checklist may be irrelevant in certain circumstances. For instance, we included in our checklist the following items under the

dimension products: 'report no defect', 'report defect', 'report how to rectify defect' etc. If the IB reports no defect, the next two items may be irrelevant unless we found contradictions. Hence, we read the entire report before making any judgement and penalising the organisation.

<sup>14</sup> Wiseman (1982) used a weighted index to measure disclosure, but in this study the items were not weighted because of potential scoring bias and scaling problems, which is consistent with Cooke (1989) and Ahmed and Nichols (1994).

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