*Environment and Planning A* 2000, volume 32, pages 1 – 8

DOI:10.1068/a3201com



## Editors announcement

The Editors are sorry to announce that Professor Paul Knox has resigned as an Editor of this journal. They would like to thank him for the extraordinary efforts he has made on behalf of the journal over the last eight years. They wish him well in his further career.

## On corporate social reporting

Ecoefficiency as a corporate interpretation of sustainability is being superseded by the incorporation of the social dimension into business. The major players could easily handle ecoefficiency. It fitted neatly into environmental reporting via the voluntary codes of ISO 14001 and environmental auditing and management systems of the EU (EMAS). It also encouraged firms to adopt better management strategies for environmental regulation, for proactive technological investment in clean technology and energy conservation, and for glossy environmental report cards aimed at assuaging shareholders and market analysts. Virtually every company worth its salt has embarked on the ecoefficiency trade, with more or less enthusiasm.

### Drivers for ecoefficiency

We shall see that meeting a social responsibility criterion is an altogether different matter, and much more demanding of the sustainability ideal. Before this issue is explored further, let us look a little more clearly at the motives for promoting ecoefficiency, because these motives spill over into corporate social reporting.

There are three primary drivers pushing for ecoefficiency.

*Regulatory intervention* is becoming more invasive, costly, and time consuming. The smart companies are seeking deals with the regulatory bodies to meet a more comprehensive 'sustainability package' that would reduce the need for expensive visits by regulatory officials to the premises. The US Environmental Protection Agency has promoted its 'xcel' approach through which companies agree to meet a portfolio of commitments 'beyond compliance'. They establish their own on-line monitoring instrumentation with a link to the local regulatory office. By mutual agreement they hire validators who take on the ISO 14001 reviews and translate them into pollution control and waste management 'packages'. And they establish an in-house management routine to accomplish this. Such an approach is looked on with some suspicion by UK counterparts, though there is certainly a push from major companies to experiment with similar procedures. Needless to say, environmental groups are also very wary. They do see an opportunity for much more explicit and interactive environmental reporting through the Internet as a result of such deals. But they are yet to accept that a corporatist approach such as 'xcel' would avoid 'regulatory capture'.

*The markets* are beginning to recognise that an ecoefficient company is also a well-managed one. In general, companies that report fully with the formal support of major environmental organisations, such as Greenpeace, the World Wide Fund for Nature, or Friends of the Earth International, now believe that they will obtain better credit ratings from analysts, and more beneficial publicity from investors and customers. This is a slowly evolving field, for markets are notoriously agnostic in the face of sustainability. But there are signs that the investment fund business is adopting a series of measures to identify ecoefficiency measures, and to advise clients accordingly.

*Brand image and reputation* count for far more than is realised in a cut-throat corporate world. The recent debacles over the flirtation between the Bank of Scotland and Pat Robinson, the opinionated US telepriest, and Marks and Spencers' child-labour scare put big holes in their customer confidence and shareholdings. So a reputation for improving the environment by obtaining more wealth from less damage is a good line for corporate reputation analysis.

All of these drivers are, of course, self-serving for business. Business is not in the world of altruism. There has to be a bottom line. And that bottom line is beginning to become a triple one (for the most cited work see Elkington, 1998).

Figure 1 summarises what appears to be at stake for the modern corporation in the coming decade. The economic element is always taken care of: that is the profit margin. The environmental element is in the regulatory arena, as discussed. The social dimension is currently truncated, but will have to grow.

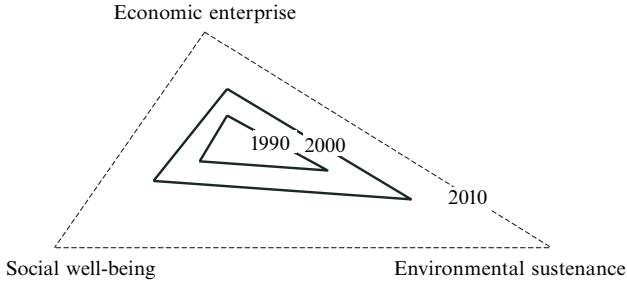


**Figure 1.** The relationship between strategies for wealth creation, environmental protection, and corporate social reporting are highly asymmetric at present. The drive is on to respond to demands for better social reporting. Will this lead to greater social justice?

**Social reporting**

Enter social reporting. This is the incorporation into the running of business of ethical, distributional, cultural considerations and aspirations for improved life chances. The stakeholders involved are citizens generally, local residents living beside manufacturing plants and supplier-chain networks, employees, and the interests of future generations. Social reporting is also driven by reputational pressures, a fear of being discovered through Internet prying, and the likelihood of massive adverse publicity resulting from any misadventure involving people and communities.

The Shell Corporation led the way with its 1978 Corporate Social Report, now updated to its 1999 Report (all on www.shell.com). BP is following, primarily with its sophisticated climate change response strategy (www.bp.com), though it will soon produce its own corporate social report. Waiting in the wings are British Telecom, Eastern Group, and Unilever. Many others will follow.

The general pattern followed by all of these companies is as follows.

(1) A group-wide sustainability council is created, linked to the board of directors and reporting direct to the chairman. This produces a greater sense of integration, and ensures that the chairman is in the thick of it. No company can move towards sustainability unless its top management is fully committed.

(2) A business manager 'report card' is generated as an annual response to meeting sustainable business principles. These are promoted through a set of indicators that are monitored through internal web sites and exposed to external scrutiny through corporate websites.

(3) Independent validation of the whole process is sought from recognised analysts who aim to criticise and encourage in roughly equal measure. Again, all this is on the corporate website.
(4) A reward mechanism is established for employee appraisal based in part on corporate social responsibility performance. How this will actually be put into effect is still in the hands of 'human resources' directors.
(5) There is a willingness to listen to stakeholder complaints and to be responsive in a definable corporate way. Again, it is too early to tell how seriously this process will be taken by high-pressure business managers.

**A critical assessment**

These are the professed ideals. In practice, no major company will be able to meet such objectives without a lot of transitional pain. Corporate cultures are simply not geared to this, nor are reward mechanisms, nor accountable responsiveness to complaints that do not have a clear business requirement. The major stumbling block will be a hostile corporate outlook that will take many years to adjust.

More to the point for environmental scientists, a whole series of difficulties face the most enthusiastic company committed to corporate social reporting.
(a) We do not really know what a 'community' is, whether it has spatial configuration, and how its trust-building networks operate. Communities vary by place, culture, and aspiration, so any standardised relationship is bound to founder.
(b) Culture affects attitudes to rights, ethics, and responsibilities. Shell is known to face a dilemma on how far to promote women managers in Islamic countries. Child labour can be a vital source of income to the impoverished family, so the task may be to make child labour safe and better linked to education, not to avoid it.
(c) Improving the well-being of vulnerable people depends on a detailed sense of their own social networks of power, influence, and informal economic functioning. That in turn requires a huge effort in sensing the anthropology and sociology of social networks and power structures. Such information does not come easily, nor reliably. In an honest attempt to find out who was 'in charge' in community positions in Equador, Arco got it all wrong (Mendez et al, 1998). The company could not discover who really spoke for the indigenous peoples, and who could be trusted when investment in local enterprises was being contemplated.
(d) Building social capital is bound to be a partnership process. Companies cannot be expected to do this on their own. They will need to formulate investment effort with a host of formal and informal organisations, virtually locality by locality. Such cultural 'fine tuning' is unlikely to be attractive to efficiency-minded managers.

**An optimistic note**

It is easy to point out obvious dangers and difficulties facing well-meaning corporations hell-bent on good corporate social reporting. The opportunist analyst will see some scope for working with such companies rather than sniping at them.

*Training for sustainability*

Outlooks, valuation techniques, intuitive methods of interviewing, partnering, and mentoring will become skills for the manager of the future sustainable corporation. These will have to be learned or taught, so there is enormous scope for interactive workshops involving environmental scientists anxious to operate in a truly interdisciplinary manner (see O'Riordan, 1999, page 10).

*Community mentoring*

The best way to discover how local social identities evolve and networks form is to link up with a number of local 'mentors' who know the culture of the inside but

can meaningfully translate it to the outside. This is also a training skill of some significance.

*Academic partnerships*
Any company looking for, say, a programme of tree planting to offset carbon dioxide emissions 'in-house' [via emissions trading or the clean development mechanism (see Grubb et al, 1999)] would be wise to contact an academic department of excellence to find out the best way to do the task with maximum social gain and least social disruption. The best departments would also be wise to discover local practitioners who have plenty of forehand experience of land rights and power networks. So there may be a triple partnership in prospect, between corporations and impacted communities, between this combination and the companies involved, and between that combination in turn and governments locally and nationally.

All this may appear too naively optimistic. Few companies have really yet shown their corporate social responsibility hand. However, the drivers mentioned earlier in this commentary are very real. There is great scope for approaching companies and sounding out pilot schemes for mutual advantage. For the corporation, good social investment now to offset a possible reputational disaster later will buy rich dividends. Think of Norst Hydro Seafoods. It has lost over 50% of its profits because of the controversy over infectious salmon amnesia in farmed salmon in Scotland. This was an avoidable calamity if the pressures to pack fish into more confined spaces had been offset by listening to the screams of the pressure groups and local people. Now Norst Hydro wants to get out of the fish farming business—but cannot find a buyer.

Tim O'Riordan

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## The East Asian banking sector—overweight?

A lot has been written about the role of the banking sector in East Asian economies. Most of the literature on the subject is devoted to Japan (Kaplan, 1997), but we can also find works on other countries of the region (World Bank, 1993). The basic conclusions of the existing research are that in East Asia the banking sectors are large relative to the size of the economies, and bank intermediation dominates other parts of the financial markets. This dominance of or reliance on banking is treated as a characteristic feature of East Asian economies and contrasts with the financial structures of Anglo-American countries.

In the 1990s the terms 'dominance' and 'reliance' have been replaced more and more frequently with the words 'overdominance' and 'overreliance'. This negative interpretation is connected with the general economic slowdown in Japan and above all with the Asian financial crisis which started in the middle of 1997. This is because the relatively large role of the banking sector, working in combination with other political and socioeconomic conditions, has been recognised as one of the major causes of the economic problems (for example, see Krugman, 1998). A simplified reasoning behind

this thesis can be presented as follows. The domination of the banking sector over the capital market implies that loan financing dominates equity financing. Personal relationships between banks and their corporate customers dominate over the anonymity of the equity market. This, in turn, contributes to 'crony' capitalism accompanied by excessive lending in often economically dubious undertakings. Such a system is very fragile. Even a relatively small shock, such as the deterioration of export conditions, caused by an appreciation of the currency or a decline of world demand, can render dubious projects bankrupt. If the amount and the scale of bankrupt undertakings are large, the domino effect amongst banks may lead entire economies into crisis.

It is not my objective in this commentary to assess the role of the banking overreliance in the East Asian crisis 1997 – 98. The above hypothetical crisis scenario simply demonstrates that overreliance is a current and significant economic issue. Therefore, it is worthwhile to investigate the type of data which was used as evidence of the considered phenomenon. At this point I would also like to make clear that I will focus on the basic, quantitative, side of overreliance.

The question can be stated thus: what kinds of measures have been used in the literature to show that the role of banking is large (or even excessive) in East Asia in relation to other countries? Three principal groups of data can be identified, each of them addressing a different aspect of the dominance issue:
(1) the relative size of the banking sector,
(2) the structure of the financial market,
(3) corporate finance.

Within the first group, we find three major macroeconomic ratios. All of them have GDP in the denominator, while the numerator constitutes the total value of bank assets (Barth et al, 1998), bank credit (Claessens and Glaessner, 1997), or bank deposits (Zahid, 1995). Using these ratios Mayer (1998), for example, describes the case of Malaysia, in which the bank credit/GDP ratio in 1993 reached 170%, approximately 3 times more than in the USA.

The second type of data involves ratios between the value of bank assets and the size of other sectors of the financial market. The latter is usually the value of outstanding corporate bonds or the capitalisation of the equity market (Barth et al, 1998). Barth states, for example, that the corporate bonds in many East Asian countries are almost nonexistent.

The third group of measures uses the language of corporate finance. The most popular are the debt to equity ratio calculated for the whole economy (Chowdhury and Islam, 1993; Wade, 1998) and other indicators of financial leverage (Pomerleano, 1998). In a 1993 report, the World Bank performed an international comparison of the share of loans in net financing sources of nonfinancial corporations, pointing out that the figure for East Asian countries is within the range of 30% to 50%, whereas for Anglo-American economies it does not exceed 20% (page 225).

The research on the relative significance of banking obviously does not stop at the above ratios and percentages. It is accompanied by analyses of the ownership structure of the banking sector, banks' corporate equity holdings, etc. However, here I am interested only in the basic methods. The reason is the following. There is a basic way to express the role of banking in East Asia compared with the rest of the world which has been neglected in the existing literature.

The suggestion is to take a look at the data presented in a magazine called *The Banker*. In the July 1997 issue we can find the list of the 1000 biggest banks in the world as at the end of 1996 (according to the USD value of capital). There are more recent bank rankings available, but the advantage of this list is that the data at this date offer a picture of world banking immediately preceding the start of the Asian crisis. If we make use of the

**Table 1.** The top twenty countries according to the number of the world biggest 1000 banks headquartered in them.

| Rank | Country | Number |
|---|---|---|
| 1 | USA | 147 |
| **2** | **Japan** | **119** |
| 3 | Germany | 84 |
| 4 | Italy | 65 |
| 5 | Spain | 38 |
| **6** | **Taiwan** | **34** |
| 7 | United Kingdom | 31 |
| **8** | **South Korea** | **30** |
| 9 | Switzerland | 28 |
| 10 | Brazil | 26 |
| 11 | Austria | 23 |
| 12 | France | 21 |
| **13** | **Hong Kong** | **17** |
| **14** | **Indonesia** | **17** |
| **15** | **Malaysia** | **16** |
| **16** | **Philippines** | **13** |
| **17** | **Thailand** | **13** |
| 18 | India | 11 |
| 19 | Mexico | 11 |
| 20 | The Netherlands | 11 |

column stating the location of bank headquarters and prepare the ranking of countries according to the number of the world's biggest banks they host, we will get table 1.

In the table we find 9 Asian, 8 European, 2 Latin American countries, and the USA. Within Europe the very strong positions of the German-speaking countries may appear surprising. Even Austria takes a very high place, in front of France! Apart from France, a surprisingly low position is occupied by the United Kingdom, especially in relation to Spain. As already mentioned, Asia leads in the category of continents. The most striking feature of the table is the massive presence of East Asian countries apart from Japan. There are 7 of them: all of the newly industrialising economies except Singapore and 4 leading emerging economies. Together they hosted 140 of the world's top banks. This means that countries creating about 5% of global GDP[(1)] were the headquarters location for 14% of the world's largest banks.

The list published by *The Banker* also allows us to prepare a ranking by city (table 2). Here, we meet 9 East Asian names, including 7 outside of Japan. The number is not surprising, because they are all simply the capitals of the countries identified in the first table. Now their positions are even higher than previously. Taipei leads the table, and quite decisively so, and 5 of its neighbours from the region qualified in the top 10. Six non-Japanese East Asian cities in the top 10 of world banking! As for the capital of Taiwan it is interesting to recall a citation from Underhill:

> "The Taiwanese state has made it an explicit goal to transform Taipei into a regional financial centre with potential to displace the status currently held by Hong Kong" (1997, page 223).

From the table it seems that Taipei has more than achieved the goal, at least in terms of numbers, surpassing not only Hong Kong but also London, Tokyo, and Paris.

The above two tables do not exhaust the potential of *The Banker*'s list. If we look, for example, at the Japanese banks we can observe many banks headquartered

[(1)] The author's estimate based on the OECD Statistical Compendium Database.

**Table 2.** The top twenty countries according to the number of the world biggest 1000 banks headquartered in them.

| Rank | City | Number |
|---|---|---|
| **1** | **Taipei** | **30** |
| 2 | London | 25 |
| **3** | **Tokyo** | **24** |
| 4 | Paris | 20 |
| **5** | **Hong Kong** | **17** |
| **6** | **Jakarta** | **17** |
| **7** | **Seoul** | **17** |
| 8 | Frankfurt | 14 |
| **9** | **Kuala Lumpur** | **14** |
| **10** | **Bangkok** | **13** |
| 11 | São Paulo | 12 |
| 12 | Vienna | 11 |
| 13 | Moscow | 10 |
| **14** | **Osaka** | **10** |
| 15 | Athens | 9 |
| **16** | **Manila** | **9** |
| 17 | New York | 9 |
| 18 | Riyadh | 9 |
| 19 | Buenos Aires | 8 |
| 20 | Lisbon | 8 |

in medium-sized, provincial cities. These are likely to be local or at most regional institutions, but they are still very large by world standards. An example is Shiga Bank in Otsu, near Kyoto which is ranked number 51 in Japan but has more capital than the biggest bank in the entire territory of the former Soviet Union.

Data analysis based on *The Banker*'s listing is obviously far from perfect. First, the ranking uses the value of capital as a criterion. Because we speak about the economic role of the banking sector, the value of assets would make a more adequate variable. Would a ranking by asset size vary considerably from the one presented above? It depends on the ratio of bank assets to capital, which varies strongly between countries. By world standards, the ratio is very high in Japan and Taiwan and low in Hong Kong, Indonesia, Malaysia, and most other East Asian states. In total, however, it should be expected to be close to the global average at the level of the region.

Second, to keep the analysis simple and different from the macroeconomic and financial measures presented at the beginning, the number of top 1000 banks by country and city was counted rather than calculating the total value of capital of the top institutions in one location. This simplification ignores the bank-size differences within the top 1000 and thus favours the locations with many banks which are big enough to qualify in the top 1000 but not necessarily the biggest. This perhaps accounts for the overwhelming supremacy of Italy and Spain over France as demonstrated in table 1. Despite this flaw I think that, as long as we do not overextend the conclusions which can be drawn from the tables, they can be used as a reasonable approximation of the institutional scene in world banking.

Why analyse the data on the location of the top banks' headquarters? I have done the exercise because information regarding the role of East Asian banks rarely considers the kind of data presented above, despite their simple and direct implications. Not even *The Banker* has bothered to write about the spatial concentration of bank headquarters. In contrast to the commonly used indicators described at the beginning, the data derived from *The Banker* do not employ directly any macroeconomic or

financial terms such as capitalisation or equity and yet offer some valuable view on the role of the East Asian banking sector.

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