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What is the benefit of ESG strategies in the Private Equity segment?

What is the impact of proactive ESG management in the Private Equity (PE) segment? And which measures can be implemented successfully in a PE portfolio?

These questions were examined by a group of researchers at EBS University, mainly Noah Bani-Harouni, together with Prof. Ulrich Hommel, together with Dr. Johannes Zuberer and Victor Linss from EY Parthenon, and Dr. Falko Paetzold, Zurich University.

It is an issue that has received little research attention in the past - which was and remains a problem for a variety of reasons. First, Private Equity has grown into a very significant investment class, which means that the relevant insights have become a priority for many investors. Second, PE investors exert very direct influence over the portfolio companies; in terms of sustainability, this is essential for providing company management with the relevant impulses. Third, the number and quality of studies examining this issue in listed markets have grown exponentially, which only highlights the gap that exists with respect to private markets.

This was the first study that combined important data sets, specifically the financial data from 102 PE companies in Europe/US, with a total of 210 funds, as well as the ESG measures of these investors as reported in the UN PRI database, and RepRisk data on controversies with regard to the 2,000 companies in the fund ("ESG footprint").

The results show that improving the ESG footprint by 50% at the fund level increases the fund's net IRR (internal rate of return) by up to 12.4%. We conducted various robustness checks, which involved the use of different financial performance indicators and the preparation of partial samples. Based on these insights, we investigated which operative ESG management instruments contribute (or do not contribute) to a successful ESG transformation. We demonstrate that centralised ESG management and the introduction of ESG value increase plans improve the ESG footprint, while increasing the ESG reporting frequency and monitoring ESG impacts do not have a significant effect.

The study closes a critical research gap in that it delivers empirical evidence for the financial advantages associated with ESG management in the PE sector. The results underline the relevance of ESG considerations in the PE sector and thus promote an understanding of the interaction between finance and sustainability.

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