



Global Private Equity Responsible Investment Survey 2023

# Generating upside from ESG: Opportunities for private equity

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**Leading PE firms have long recognised that managing ESG factors helps create value. Our new survey shows most firms agree, seeing no conflict between ESG and returns. Here, we look at the industry’s evolving approach—and highlight prospects for further gains.**

by Eric Janson, Miriam Pozza, Leonie Schreve and Darice Caudle

Ten years ago, when PwC first surveyed private equity (PE) firms on their approach to environmental, social and governance (ESG) topics, risk management was their foremost concern. Now their outlook has changed. Our latest survey, of more than 150 PE houses, shows, first, that respondents overwhelmingly believe that ESG management can help create value. Some 70% place value creation among the top three drivers for their organisation’s ESG activities. Second, the survey findings indicate that it is standard practice for PE firms to consider ESG factors when sourcing opportunities, carrying out due diligence, forming post-acquisition plans and deciding on deal terms.

When asked about the benefits of ESG activities, respondents shared a range of views. A third set of findings suggests that PE organisations are more likely to report qualitative outcomes—which are typically associated with value creation, including higher exit multiples—than to report directly measurable financial impacts. More than half of respondents identify brand enhancement, risk mitigation, competitive differentiation and client attraction as ESG’s main benefits to their organisation. Less than one-fifth identify revenue growth and cost efficiency. These findings may also reflect the challenge of precisely attributing financial value to ESG considerations. Only a third of respondents say their organisation incorporates ESG factors into valuation exercises, which we see as essential to confirming that ESG can be a value driver on a given deal.

Experience has also shown that leading firms bring ESG considerations into their investment decisions, specifying ESG-related opportunities as they define their deal theses. To conclude this report, we’ll describe four areas in which using an ESG lens can help firms locate potential sources of added value.



## Most PE firms aim to create value with ESG

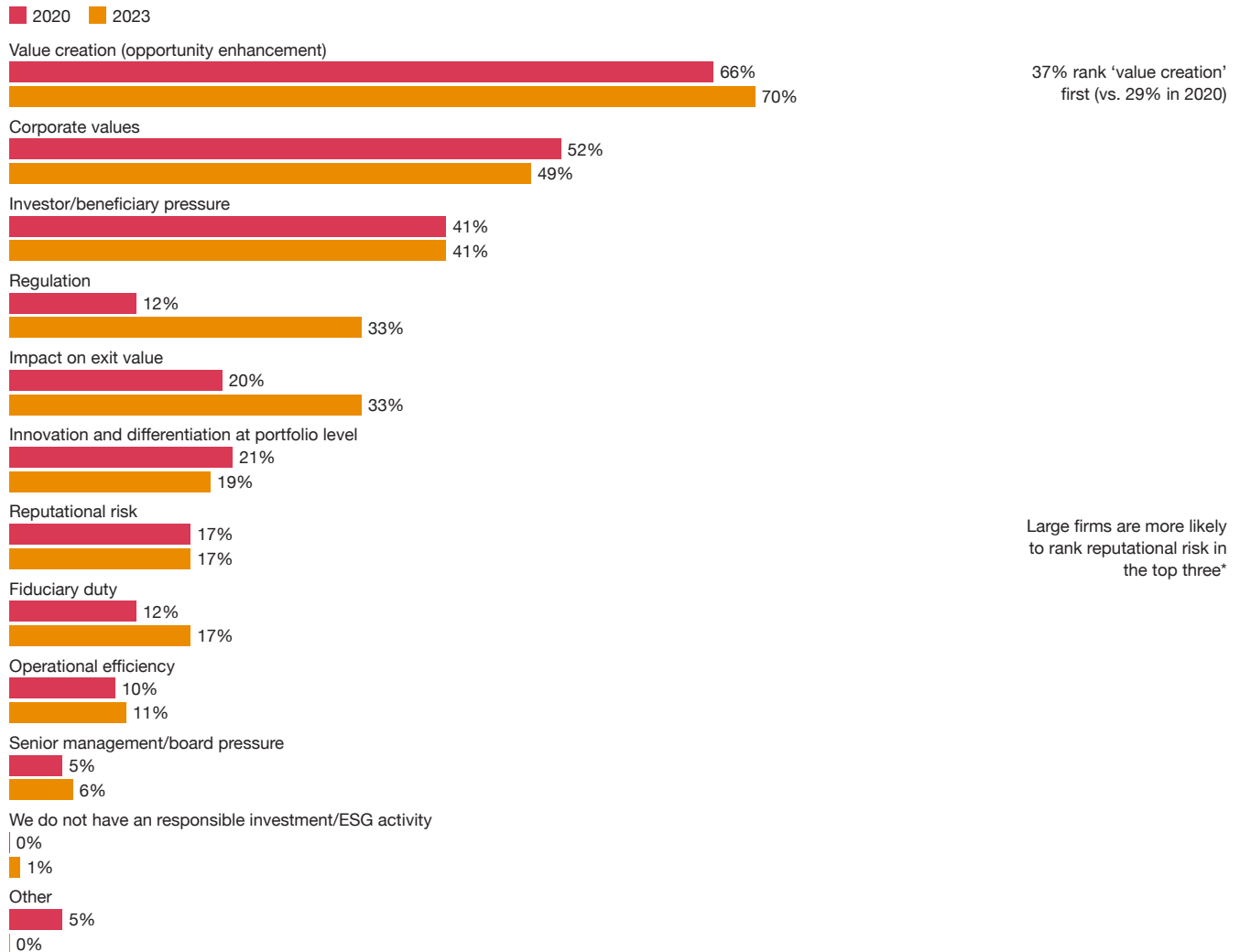
By and large, survey respondents say they see ESG management as consistent with their overall efforts to generate returns for clients. More than 80% say that considering ESG performance is ‘in line with the pursuit of returns,’ compared with just 1% who say it is ‘in conflict with the pursuit of returns.’

A large majority of respondents, 70%, rank value creation as one of the top three drivers for their ESG activities. Although this tally was similar in 2020, when it was 66%, we find that this year’s respondents are more likely to put value creation first on their list of ESG drivers: 37% do so, compared with 29% in 2020.

Noteworthy, too, are the upticks in the share of respondents who cite ‘regulation’ and ‘impact on exit value’ as motives driving action on ESG. Though the numbers are small, we also observe an increase in the share of respondents who place ‘fiduciary duty’ among their top three drivers (see chart, next page).

# Value creation is the top driver for ESG activity in private equity; regulation and impact on exit value have risen in importance since our last survey

Share of respondents ranking each driver among the top three for their firm/fund



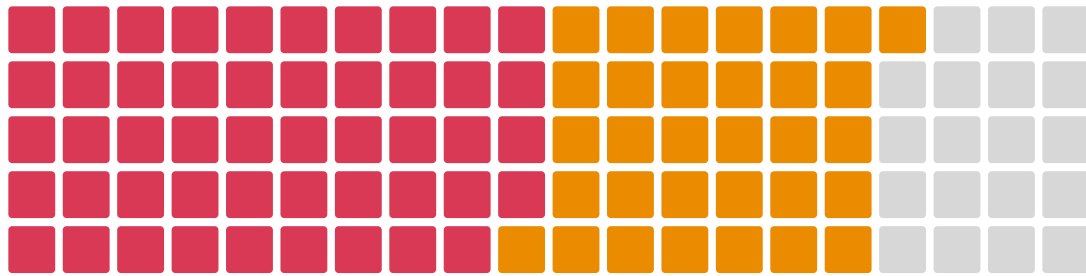
\*36% of firms with US\$10.1 billion or more of assets under management; 44% of firms with 101 or more portfolio companies. Source: PwC's Global Private Equity Responsible Investment Survey 2023 (base: all respondents = 166)

We also asked respondents how many of their recent deals featured ESG activity as a primary driver of value creation. One-third report that more than 50% of their deals did so. Nearly half indicate that at least some deals included ESG considerations as a main value driver. Although our survey didn't dig further, experience suggests that PE firms could use ESG analysis to define additional opportunities for value creation—some of which we'll discuss later in the report—that conventional analysis might overlook (see chart, next page).

# One-third of PE respondents say that ESG was a primary driver of value creation in more than half of their organisation's recent deals

Of the deals that your firm/fund completed during the last 12 months, what proportion included ESG as one of the primary drivers of value creation?

- 49% of respondents says '1-50% of deals'
- 32% of respondents says '51-100% of deals'

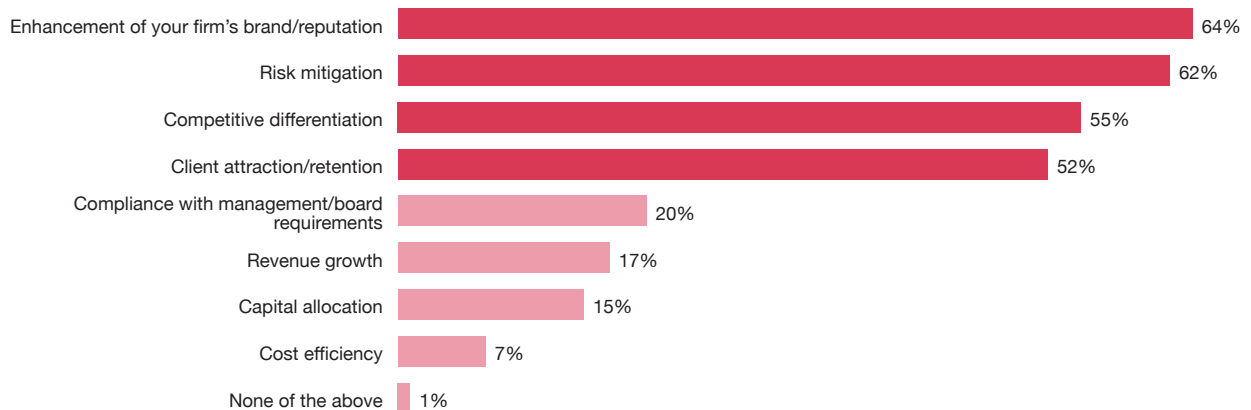


Source: PwC's Global Private Equity Responsible Investment Survey 2023 (base: all respondents = 166)

More than half of respondents say that managing ESG topics has four benefits—all of which can be linked to value creation, in our experience. One of these benefits is risk mitigation, which 62% of respondents place among their top three choices. The other three pertain to a firm's standing in the market: 'enhancement of your firm's brand/reputation' (64%), 'competitive differentiation' (55%) and 'client attraction/retention' (52%; see chart).

## PE firms are most likely to say that ESG's benefits relate to market positioning and risk mitigation

Share of respondents ranking each benefit of ESG among the top three for their firm/fund



Source: PwC's Global Private Equity Responsible Investment Survey 2023 (base: all respondents = 166)

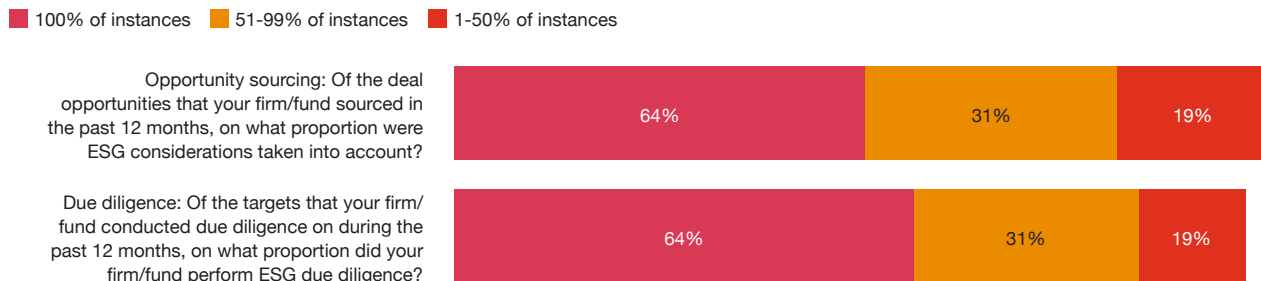


## Many PE firms embed ESG in core activities

This year’s survey also highlights those ESG practices that have seen enough uptake among PE firms to count as industry standards. These practices focus on the opening and closing stages of the deal life cycle. More than half of survey respondents say that they looked at ESG factors when sourcing all their deals and when performing all their due diligence reviews during the past 12 months (see chart).

## PE firms regularly look at ESG factors when sourcing opportunities and performing due diligence

Share of respondents citing each proportion of instances where ESG is considered



Note: Percentages shown may not total 100 due to rounding.  
 Source: PwC’s Global Private Equity Responsible Investment Survey 2023 (base: all respondents = 166)

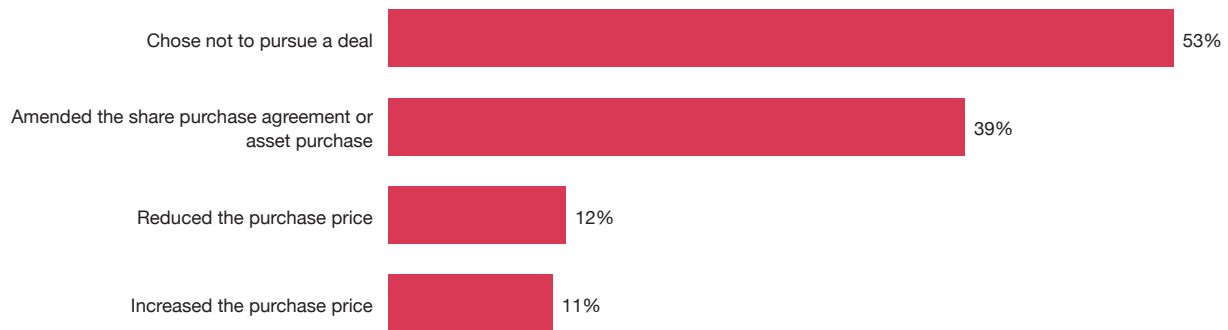
It’s about as common for PE firms to incorporate ESG topics into the post-acquisition plans for their new holdings, according to the survey. (Experience suggests that the work performed prior to and during due diligence, in line with firms’ ESG commitments, often generates ideas used in post-acquisition plans.) Another question registered an increase in the share of respondents who say their firms integrate ESG-related risks and opportunities into transformation plans, either systematically or on an ad hoc basis. That share topped 90% in this year’s survey—up from 73% in 2020.

Given that level of attention, perhaps it's not surprising that PE firms seem to take care to avoid ESG risks. When we asked respondents how frequently, during the last 12 months, their firm changed its approach to a deal because of ESG considerations, 53% of respondents say their firm chose not to pursue a deal at least once. (By comparison, 56% of respondents to the 2020 survey said they had at least once refused to enter an agreement with a general partner or turned down a potential investment on ESG grounds.) Around four in ten say their organisation amended the share purchase agreement in at least one instance (see chart).

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## PE firms frequently choose not to pursue deals because of ESG factors

Share of respondents who say at least one deal changed because of ESG factors in the previous 12 months



Source: PwC's Global Private Equity Responsible Investment Survey 2023 (base: all respondents = 166)

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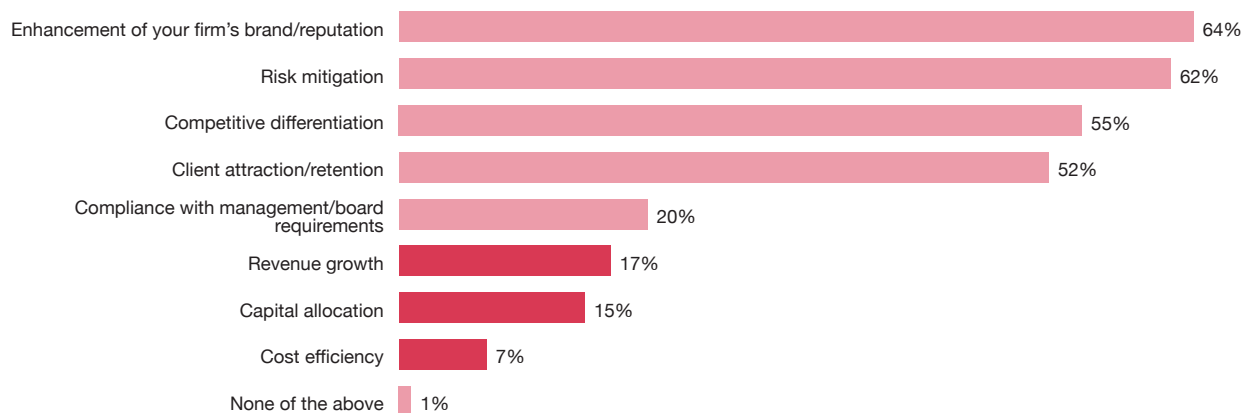
## Few PE firms highlight ESG's financial benefits—but valuation may be a challenge

Asked to identify the top three benefits of their ESG activities, respondents are more likely to name qualitative outcomes such as competitive differentiation and brand enhancement, which in our experience are often associated with stronger financial performance, than to name direct financial outcomes. Less than 20% of respondents select revenue growth, capital allocation or cost efficiency as one of the top three benefits that ESG activities bring to their firm or fund (see chart).

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### Relatively few PE respondents say that ESG activities support their organisation's growth, capital allocation or cost efficiency

Share of respondents ranking each benefit of ESG among the top three for their firm/fund



Source: PwC's Global Private Equity Responsible Investment Survey 2023 (base: all respondents = 166)

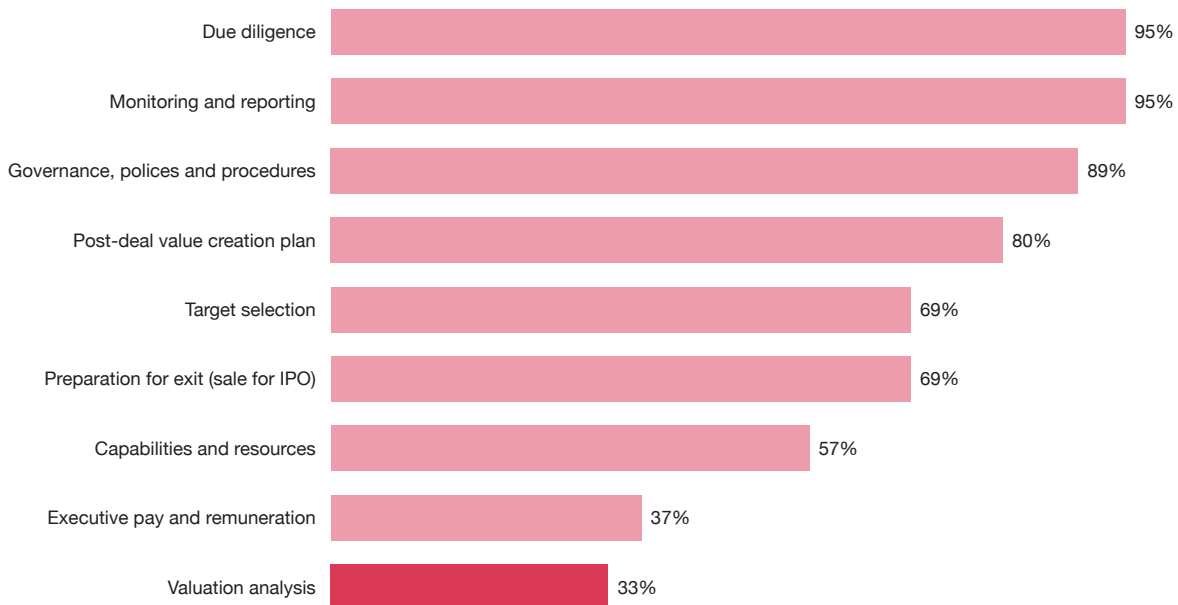


Yet it might be hard for PE firms to tell how much financial value they are getting from ESG efforts, even when they spot opportunities. In our experience, firms recognise that addressing ESG-related factors—whether by seeking improvements in sustainability performance, by pivoting towards growing markets for sustainable products and services, or by other means—can have a positive impact on a target company’s cash flows, cost of debt and terminal value. However, we’ve also observed that a lack of data can limit PE firms’ ability to attribute value creation specifically to their work on these ESG-related factors. And in fact, only one-third of respondents to our survey say that their firm or fund integrates ESG considerations into valuation analysis. By contrast, nearly all respondents say their organisation integrates ESG considerations with due diligence (see chart).

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## Only one-third of PE respondents say their organisation embeds ESG into valuation analysis

Share of respondents who say their firm/fund integrates ESG considerations in each activity



Source: PwC’s Global Private Equity Responsible Investment Survey 2023 (base: all respondents = 166)

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## Firms are taking on ESG topics

To gauge the relevance of 21 specific ESG topics, our survey asked respondents about the extent to which their organisation recognises these topics as material and takes action to manage them.

Within the environmental, social and governance categories, several noteworthy patterns and findings also emerge (see charts, next pages).

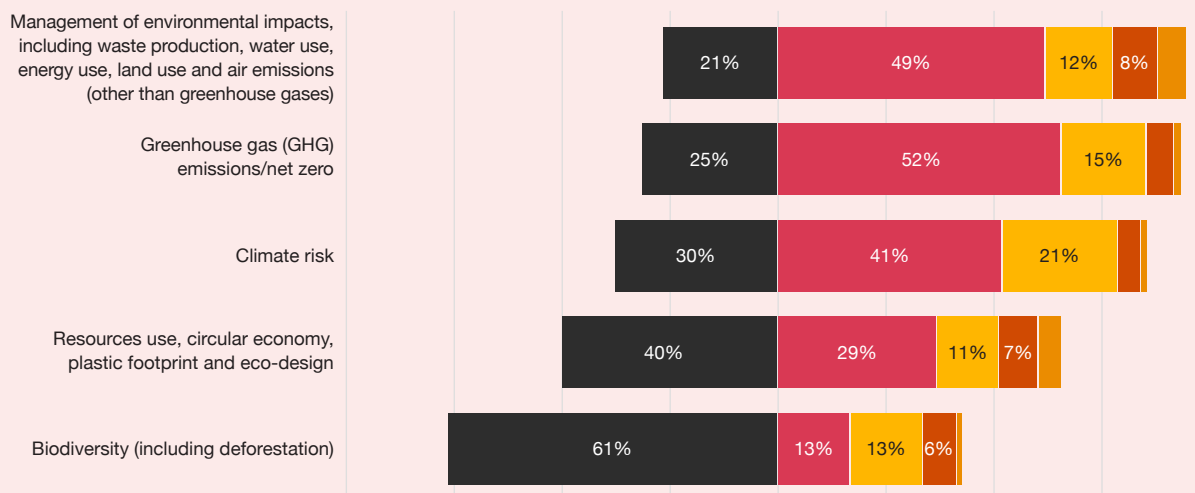
**Climate commands attention.** Seventy percent or more of respondents say their organisation sees greenhouse gas emissions and climate risk as material topics, along with the management of environmental impacts.

**Biodiversity bears watching.** Although the share of respondents who identify biodiversity as material remained about the same as in 2020, more of those respondents (34% versus 27%) say their organisation plans to address it in the coming year.

**Social and governance topics galvanise action.** We asked respondents about 16 social and governance topics. On ten of them, more than 70% of respondents say their organisation sees them as material, and more than 50% say their organisation has already taken action.

## Environmental topics

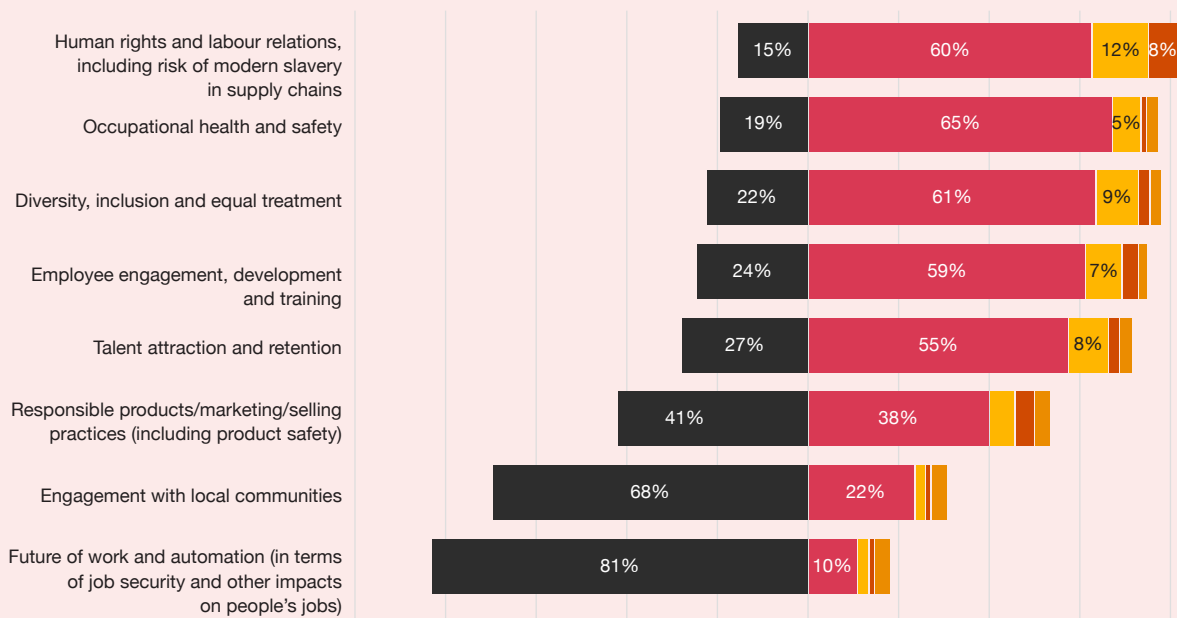
■ Topic is not material  
 ■ We have already implemented measures  
 ■ We are implementing measures within the next year  
■ We plan to implement measures in the next 2 to 3 years  
 ■ We do not plan to implement measures



Source: PwC's Global Private Equity Responsible Investment Survey 2023 (base: 165)

## Social topics

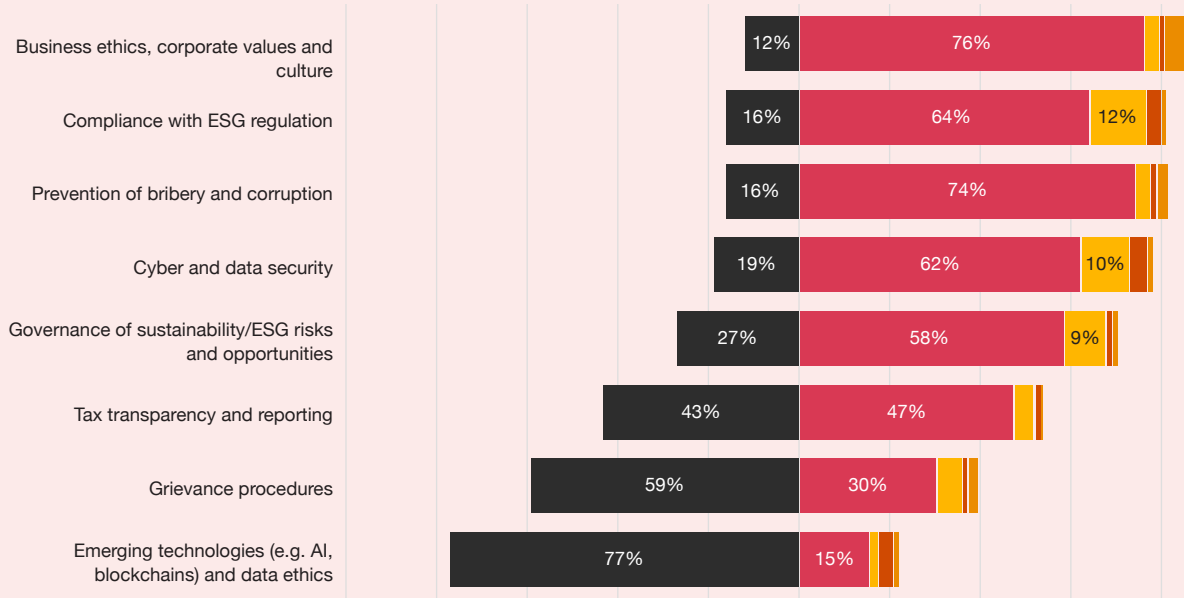
■ Topic is not material  
 ■ We have already implemented measures  
 ■ We are implementing measures within the next year  
■ We plan to implement measures in the next 2 to 3 years  
 ■ We do not plan to implement measures



Source: PwC's Global Private Equity Responsible Investment Survey 2023 (base: 165)

## Governance topics

Topic is not material
  We have already implemented measures
  We are implementing measures within the next year
  We plan to implement measures in the next 2 to 3 years
  We do not plan to implement measures



Source: PwC's Global Private Equity Responsible Investment Survey 2023 (base: 165)



## Seeking ESG's value throughout the deal life cycle

Our surveys show that PE firms have come to regard the sustainability agenda less as a source of risk and more as a wellspring of value. Many are also integrating ESG factors into core activities such as due diligence. What sets leading firms apart, in our experience, is that they identify and pursue ESG-related opportunities at every stage of a deal, from targeting to exit. Here, we set out four practices that can orientate PE investors towards more potential for value creation.

**Explore investments in underfunded industries and geographies to establish sustainable deal flow.** As businesses and governments step up their efforts to achieve net-zero emissions and other ESG-related goals, new markets for sustainable goods and services should emerge—and enterprises serving those markets will need financial backing. For example, PwC research shows a misalignment in funding for climate-technology ventures: sectors that account for 85% of global greenhouse gas emissions receive just 52% of climate-tech investment. Other PwC research shows that the bulk of financing for green infrastructure flows into developed countries—even though developing regions such as Africa and Southeast Asia have both significant capital requirements and a high degree of “investability.” It’s in gaps such as these where PE firms may find promising opportunities for value creation—especially in sectors, such as infrastructure, where gains accrue over long time horizons.

**Factor sustainability into the exit strategy—before making the deal.** When planning how they’ll maximise exit returns, PE firms should recognise upfront that companies with strong ESG credentials can yield a premium. After all, ESG investing is on the rise: one recent PwC study projected that ESG assets under management (AuM) would grow from 14.4% of total AuM in 2021 to 21.5% in 2026. And PwC’s 2022 Global Investor Survey found that

most investors want companies to report the relevance of sustainability factors to their business model. PE firms can create more value by defining, for each target company, a superior ESG profile in terms of impact on the environment and society as well as alignment with sustainability-related market shifts and regulation. Then they can determine what changes are needed for a target to achieve such a profile, and work on those changes over the holding period so that the company is well prepared for an ESG-enhanced exit.

**Look for green incentives and tax savings early in the deal-structuring process.** In line with the environmental and social goals noted above, many governments are using green incentives and environmental taxes to encourage businesses to change their behaviours. The European Green Deal, for instance, includes more than 1,000 new or modified levies. In the United States, the Inflation Reduction Act sets out nearly US\$370 billion in provisions related to climate change and clean energy. To create additional value, PE firms will want to determine how these policies and programmes apply to a given deal, and then design tax structures that allow them to access the full complement of credits and incentives. One large energy-technology company, for example, found that incentives could pay for up to 50% of the costs of its decarbonisation initiatives.

**Consider creative financing structures that use low-cost green capital.** Another PwC study projected that issuance of green, social and sustainability (GSS) bonds in Europe could increase from €500 billion in 2021 to €1.4 trillion or even more in 2026. PE firms should be mindful of opportunities to finance deals with low-cost green capital, such as sustainability-linked loans (SLLs). Our latest survey suggests that this is not yet common: only half of respondents say their organisation used SLLs or other ESG-related financing on at least one deal in the previous 12 months. Other potential sources of financing for sustainability-centred deals include the transition funds—that is, funds explicitly dedicated to helping companies achieve their emissions-reduction targets—that some large financial institutions are setting up.

As the transition to a sustainable economy progresses, more and more value-creation opportunities will emerge. Focusing on these prospects will help PE firms deliver the strong returns that their investors seek.

# Methodology

The Global Private Equity Responsible Investment Survey explores the views of executives and senior investment and sustainability professionals at private equity firms. Between March and May of 2023, PwC surveyed 166 respondents in 22 countries and territories across Africa, the Americas, Asia-Pacific, Europe and the Middle East. Among the respondents:

- 135 identify themselves as general partners, three as limited partners and 19 as both; eight answer 'not applicable.'
- 9% represent organisations with US\$200 million or less of assets under management (AuM), 30% represent organisations with US\$201 million–US\$1 billion of AuM, 37% represent organisations with US\$1.1 billion–US\$10 billion of AuM, 13% represent organisations with US\$10.1 billion–US\$50 billion of AuM, and 10% represent organisations with more than US\$50 billion of AuM.
- 15% say their firm has a portfolio of ten or fewer companies, 30% say 11–20 companies, 28% say 21–50 companies, 7% say 51–100 companies, 5% say 101–150 companies, and 14% say 151 or more companies.
- 26% represent organisations with a small-cap investment approach, 56% represent organisations with a medium-cap investment approach, and 7% represent organisations with a large-cap investment approach; 11% answer 'not applicable.'

Percentages shown may not total 100 due to rounding.

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