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Sustainability and ESG

What are their implications for private equity investors?

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2023 Q4

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How are ESG and Sustainability related?

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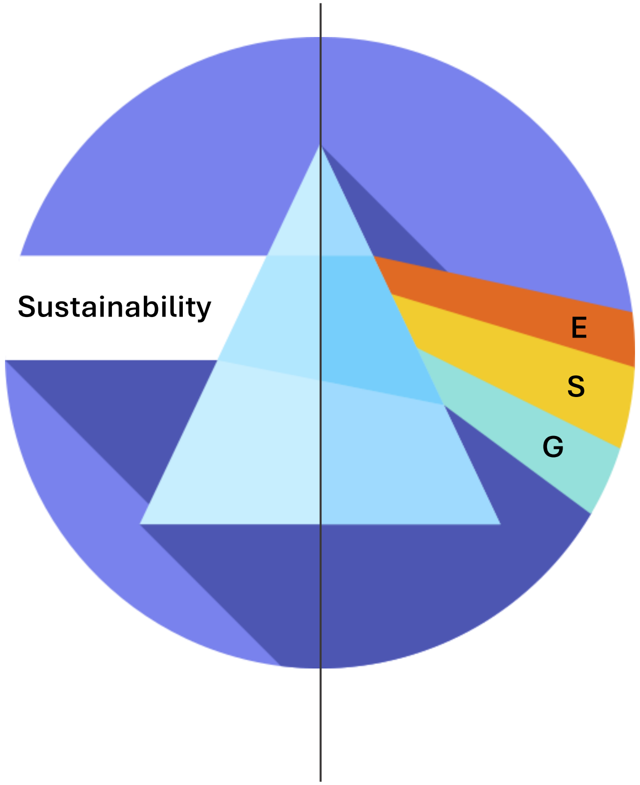
Sustainability and ESG share the same goal of long-term development, and can be “used interchangeably” despite their unique intricacies

Sustainability

“Sustainability is the overarching philosophy”

- Sustainability is the **practice of operating a business** in a way that meets the economic, social and environmental needs of the present without compromising the **ability of future generations to meet their own needs**
- Sustainability represents a **broader principle** that encompasses responsible and ethical business practices in a **holistic manner, without specific KPIs**
- It provides an **umbrella for ESG**, with an interplay between environmental and corporate sustainability



ESG

“ESG is a lens, tool or framework for Sustainability”

- ESG is a **set of criteria used to evaluate environmental (E), social (S), and governance (G) factors**
- It can be thought as a **subset of sustainability** which includes economic consideration. Its main purpose is to **provide stakeholders and investors with a framework** to assess a company's impact on society and the environment, as well as its corporate governance practices
- It can be a **risk management tool**, **investment lens**, or KPIs to determine **corporate rating** or **executive pay**

ESG looks at **how the “world” impacts a company or investment**, whereas sustainability focuses on **how a “company or investment” impacts the world**

Source: HSBC, Calista team research

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The PE fund industry

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ESG fund sizes have become non-negligible and there are still a lot of nuances and themes for investor to tick the right boxes

The largest 25 ESG PE funds raised in the last 10 years, with Permira, EQT, and Brookfield dominating the rank

See details in the following pages

Rank	Name	Manager	Year	Capital raised (bn)	Type
1	Permira VIII	Permira Advisers	2023	€16.70	Article 8
2	EQT IX	EQT	2021	€15.60	Article 8
3	Brookfield Global Transition Fund	Brookfiel Asset Management	2022	$15.00	Impact
4	Baring Asia PE fund VIII	BPEA EQT Asia	2022	$11.20	Article 8
5	Hg Saturn 3	Hg	2022	$11.06	Article 8
6	EQT VIII	EQT	2018	€10.75	Article 8
7	TPG Rise Climate Fund	TPG	2022	$7.30	Impact
8	EQT VII	EQT	2015	€6.82	Article 8
9	Hg Genesis 10	Hg	2023	€6.75	Article 8
10	Ardian Buyout Fund VII	Ardian	2021	€6.50	Article 8
11	Ardian Private debt V	Ardian	2022	€5.00	Article 8
12	Astorg VII	Astorg	2019	€4.24	Article 8
13	BeyondNetZero Fund I	General Atlantic	2022	$3.50	Article 9
14	MED Platform II	Archimed	2023	€3.00	Article 9
15	KKR Global Impact Fund II	KKR	2023	$2.80	Impact
16	The Rise Fund III	TPG	2023	$2.70	Impact & Article 9
17	Summa Equity Fund III	Summa Equity	2022	€2.30	Impact & Article 9
18	The Rise Fund II	TPG	2018	$2.17	Impact
19	The Rise Fund	TPG	2017	$2.00	Impact
20	Generation IM Sustainable Solutions Fund IV	Generation Investment Management	2022	$1.70	Article 9
21	Horizon Environment and Climate Solutions I	Goldman Sachs Asset Management	2023	$1.60	Impact & Article 9
22	Ambienta IV	Ambienta SGR	2022	€1.55	Article 9
23	Climate Assets Fund I	Generation Investment Management	2023	$1.50	Article 9
24	T2 Energy Transition Fund	Tikehau Capital	2021	€1.14	Article 9
25	Eiffel Energy Transition III	Eiffel	2022	€1.00	Article 9

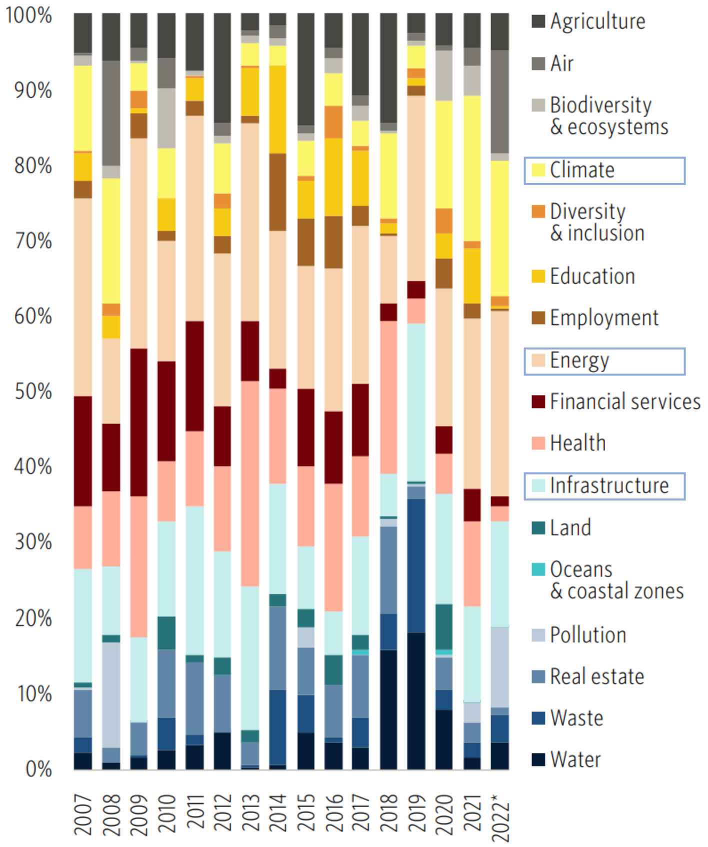
Article 6: It covers funds which do not integrate sustainability and can include tobacco or thermal coal equity, labelled as **non-sustainable** under SFDR

Article 8: Also known as "environmental and socially promoting", it is the **entry level to claim ESG ("light green")** under current SFDR framework

Article 9: Also known as "products targeting sustainable investments", it represent the **most stringent level ("dark green") for funds to claim ESG or impact**

Impact: Not officially below any "Article" of SDFR, it could be **self-claimed** but generally following **SGDs** for strategy and **IRIS+** for measurement tool

Climate, Energy, and Infra are key fund themes of total capital raised in the impact category



Source: New Private Markets, Pitchbook, SFDR, GIIN; Note: As of 2023, the European Commission has launched a consultation into a possible shift away from Article 8 and 9 fund classifications to revamp fund regulations

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Zoom on Family Offices

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Despite a strong interest in aligning with current ESG trends, most Family Offices are still moving slowly towards a meaningful ESG allocation

What do they do?

- A family office is a **private wealth management firm** established by an ultra-high-net-worth family that provides that family with a selection of personalized services including investment management, financial and tax planning and philanthropic initiatives, **usually across generations**
- More and more family offices are **integrating ESG concerns** into their investment strategy, whether that be through **direct investments** in businesses with sustainable business models, screening of **listed equities**, or through investing in **externally managed funds** with ESG mandates, amongst other strategies

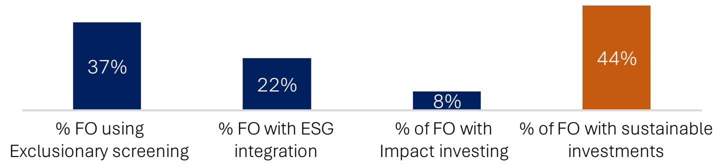
What are their consideration of ESG?

Why ESG?	▪ Long-term development aligned with ESG timeframe – holistic view ▪ Wealth preservation in a sustainable future ▪ Increasingly stronger push from the second generation ▪ Alternatives to pure philanthropy ▪ Greater autonomy to allocate to ESG initiatives, or as pioneer
Why not ESG?	▪ There is no strict obligation due to private wealth ▪ No external shareholder pressure ▪ Lack of inhouse capabilities to fully address ESG ▪ Potentially often associated with smaller ticket size ▪ Difficult to find a GP with same sustainable investment goal

What is their response to ESG investing?

- According to **UBS 2023 global survey**, family offices **willing to consider ESG** for their allocation are still **not majority, only 44% among all**
- Due to their discretion and varied size, there could be **polarization** on their reaction to ESG allocation

UBS 2023 Global FO survey



What should they expect from ESG?

- Family offices can have **multiple roles – fund allocator, direct investor, business builder, and wealth owner**, and they consequently have to look at ESG from different angles
- They should become **more holistic** in terms of their response to ESG and recognize their **accountability across the value chain**

Chain of Accountability

Beneficiaries | Asset Owner | Fund Manager | Corporate Board | Management | Workforce

← Flow of Accountability

Key players

JAB, Stonehage Fleming, Pathstone Federal Street, kedge capital, Jordan Park, Bluehaven Initiative, KIRKBI, JM Family Enterprises, Inc., KL Felicitas Foundation, Caprock

Focus on key family offices, or HNWIs actively engaged in ESG

Source: UBS, New Private Markets, Calista analysis

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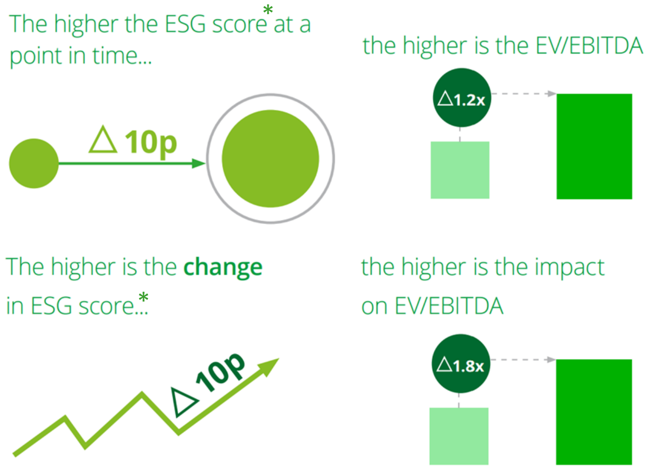
Is there really a green premium?

Green premium has been the most concrete upside that investors would expect from the ESG investment thesis

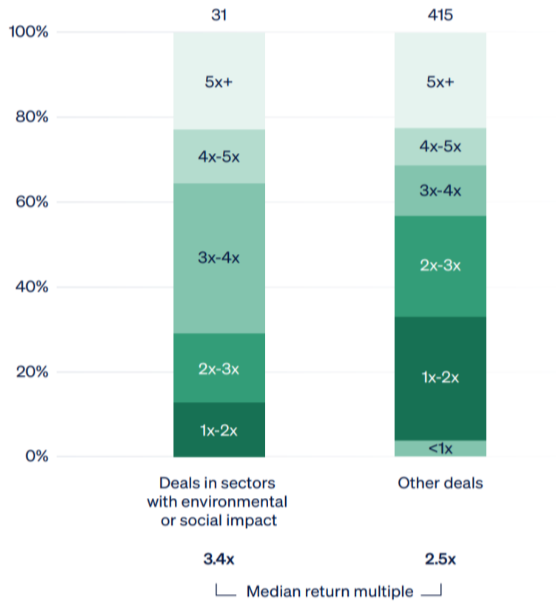
Studies support the existence of ESG premium

- As PE firms have the ability to **employ capital directly**, and in a focused manner towards specific ESG goals, they can exercise their **influence over leadership positions** to drive varying degrees of ESG initiatives
- The **financial benefits** of ESG integration are most reflected in the **Exit value**, often associated with **"green premium" or "ESG value premium"**, which has been substantiated by a Deloitte study

Deloitte 2022 Study on ESG value premium (EV/EBITDA)



Bain & Company Study on APAC 2014-2018 PE-led exits (MOIC)



- Bain & Company also found that the **median multiple on invested capital** was **3.4x** for deals with social and environmental impact, compared with **2.5x** for other deals, presenting a **0.9x increase of the multiple**

How ESG is driving the value?

	Value creation	Risk mitigation
Portfolio company level	**Sales boost** as consumers are attracted to sustainable products Increased **employee productivity** **Innovation** pushed by new solutions, regulations or governmental initiatives	**Lower operating costs** when aligned with best ESG practices Less **government interference** Decreased **cost of capital** when ESG measures improve
Investment firm level	Potentially **Increasing investment returns** Giving investment professionals **more tools** and techniques to use in analysis Improving the **quality of engagement** and stewardship activities	Meeting requirements under **fiduciary duty or regulations** Meeting client and **beneficiary demands** **Lowering investment risk** **Reputational risk** at a firm level and investment level

Source: Moonfare; Deloitte "Does a company's ESG score have a measurable impact on its market value?"; Note: *ESG score is based on Refinitiv data in the Deloitte study

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Glossary

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AI	Artificial Intelligence
AUM	Assets Under Management
CAGR	Compounded Annual Growth Rate
CCUS	Carbon Capture, Utilization, and Storage
CDP	Carbon Disclosure Project
COP	Conference Of the Parties (United Nations Climate Change Conference)
CSR	Corporate Social Responsibility
DER	Distributed Energy Resources
DFI	Development Finance Institution
EBITDA	Earnings Before Interest, Tax, Depreciation and Amortisation
EIA	Environmental Impact Analysis
ESG	Environmental, Social and Governace
EV	Enterprise Value
GHG	Greenhouse Gas
GIIN	Global Impact Investing Networw
GP	General Partner
GSIA	Gyumnwan River Environmental Impact Assessment
ILPA	Institutional Limited Partners Association
IPCC	Intergovernmental Panel on Climate Change
KPI	Key Performance Indicator
LP	Limited Partner

LTV	Loan-To-Value
MOIC	Multiple On Invested Capital
OECD	Organization for Economic Co-operation and Development
PE	Private Equity
PG&E	Pacific Gas & Electric Company
PR	Public Relations
PRI	Principles of Responsible Investing
RE	Real Estate
RI	Responsible Investing
SBTI	Science Based Targets Initiative
SDG	Sustainable Development Goals
SFDR	Sustainable Finance Disclosure Regulation
SRI	Socially Responsible Investing
TCFD	Task Force on Climate-Related Financial Disclosures
UN	United Nations
UNGC	United Nations Global Compact
US	United States of America
USD	United States Dollar
US SEC	U.S. Securities and Exchange Commission
WRI	World Resources Institute
WWF	World Wildlife Fund

Source: Calista team

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