EXAMINING THE PRIVATE EQUITY INDUSTRY'S REACTION TO COVID-19 THROUGH AN ESG LENS

By Lee Godfrey, Managing Director, Western Europe at Intertrust Luxembourg

As the private equity industry continues to adjust to the unprecedented challenges of COVID-19, the economic impact of this global healthcare crisis raises many questions about how companies will manage their social and human capital. In a recent webinar hosted by Intertrust, important questions were raised about the pandemic's long-term impact on environmental, social and governance (ESG) issues facing both General Partners (GPs) and Limited Partners (LPs). For example, could the COVID-19 crisis accelerate the trend for a more sustainable approach to investing?

In our recent Global Private Equity Outlook 2020 report, over half of private equity fund managers see the environment for the sector deteriorating over the next twelve months. Despite the obstacles ahead facing a profoundly altered market struck by the slowdown in fundraising and deal-making, Rajaa Mekouar, CEO of Luxembourg Private Equity & Venture Capital Association believes that the private equity industry should "rise up to the challenge of demonstrating its value-add by helping to preserve jobs and fostering innovation."

Sachin Vankalas, General Manager of Luxembourg Finance Labelling Agency, believes that the current slowdown might embolden GPs to re-examine the way they do business and how they approach sustainability. Vankalas has argued that the crisis shines a spotlight on the "S" in ESG, with social issues becoming an increasingly urgent consideration for companies throughout these difficult times. "COVID pushes companies to start thinking about very basic questions, such as the health and safety of employees, contingency plans and disaster management preparedness. These are factors that ESG has been shining a light on for years, highlighting the importance of firms knowing their assets better and understanding their environmental impact."

In recent years, companies have shifted away from the traditional focus on shareholder value above everything else. According to Rajaa Mekouar, the magnitude of the pandemic has only accelerated this trend: "the private equity industry needs to shift from a shareholder value perspective to a broader focus on its stakeholders. Paradoxically the impact of the COVID-19 crisis may lead to the private equity industry adopting a more proactive role towards ESG and the more positive data showing the link to positive financial performance, the sooner GPs will incorporate environmental and social issues in their investment decisions."

Although support for the Principles of Responsible Investment (PRI) has grown over the past five years, nearly half of private equity managers (49%) believe the implementation of ESG by GPs is being hampered by a lack of consistent reporting standards. Abdel Hmitti, Head of EMEA, Private Equity & Real Asset Services at State Street, argues that as LPs request more frequent and transparent reporting from private equity managers, it won't be long before we see a more standardised and consistent approach to ESG reporting. Mekouar adds that as the shifts in consumer behaviour become increasingly apparent, she expects LPs to spearhead the push towards the adoption of ESG standards.

In summary, while hurdles still remain to be cleared, the pandemic has only heightened the urgency of educating advisers on the importance of incorporating ESG factors into client portfolios, if sustainable and ethical investment is to continue to accelerate its march into the mainstream.

To download a copy of the Global Private Equity Outlook 2020 report, please **click here**.