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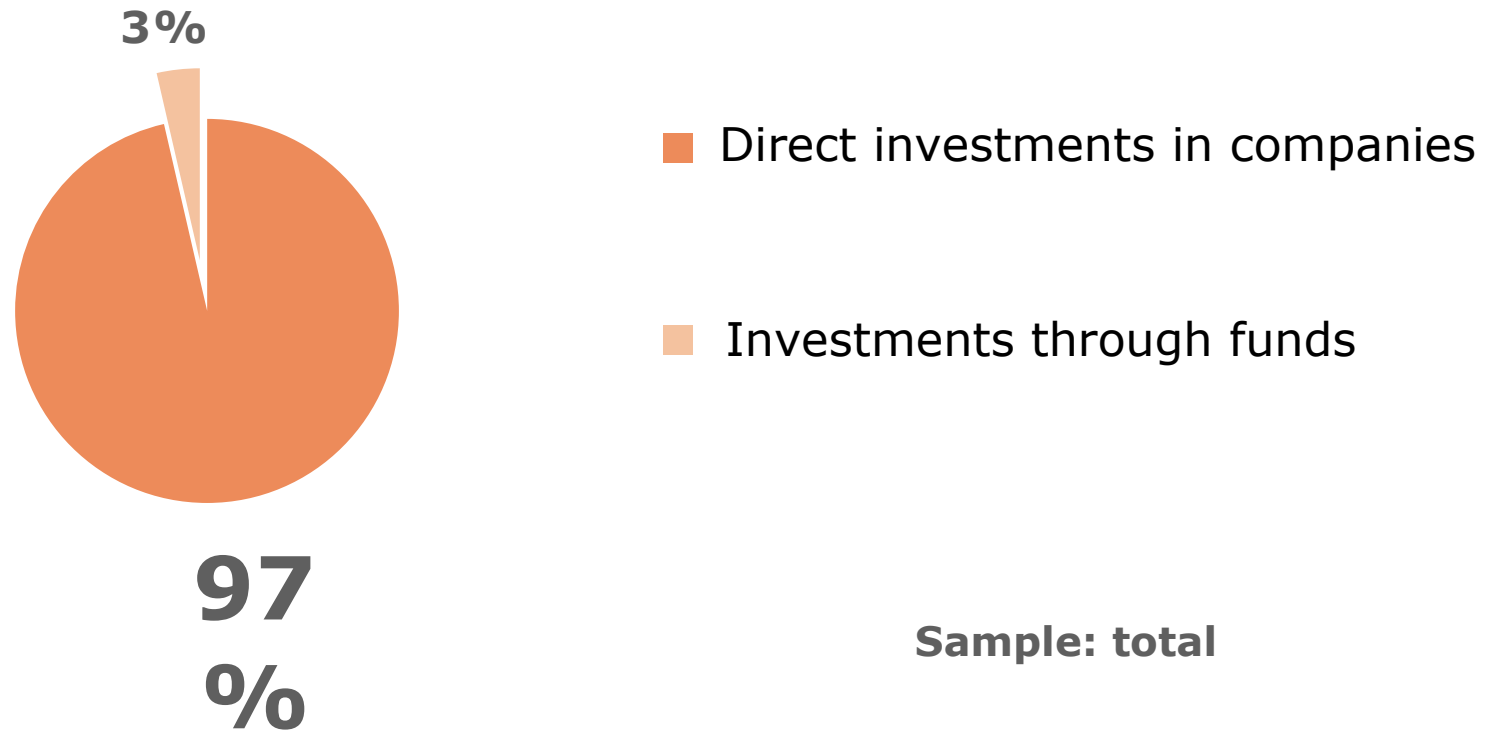
WHAT DO PRIVATE EQUITY INVESTORS THINK OF THE INTEGRATION OF ESG CRITERIA?

Survey conducted by Novethic SRI research centre
7 July 2009

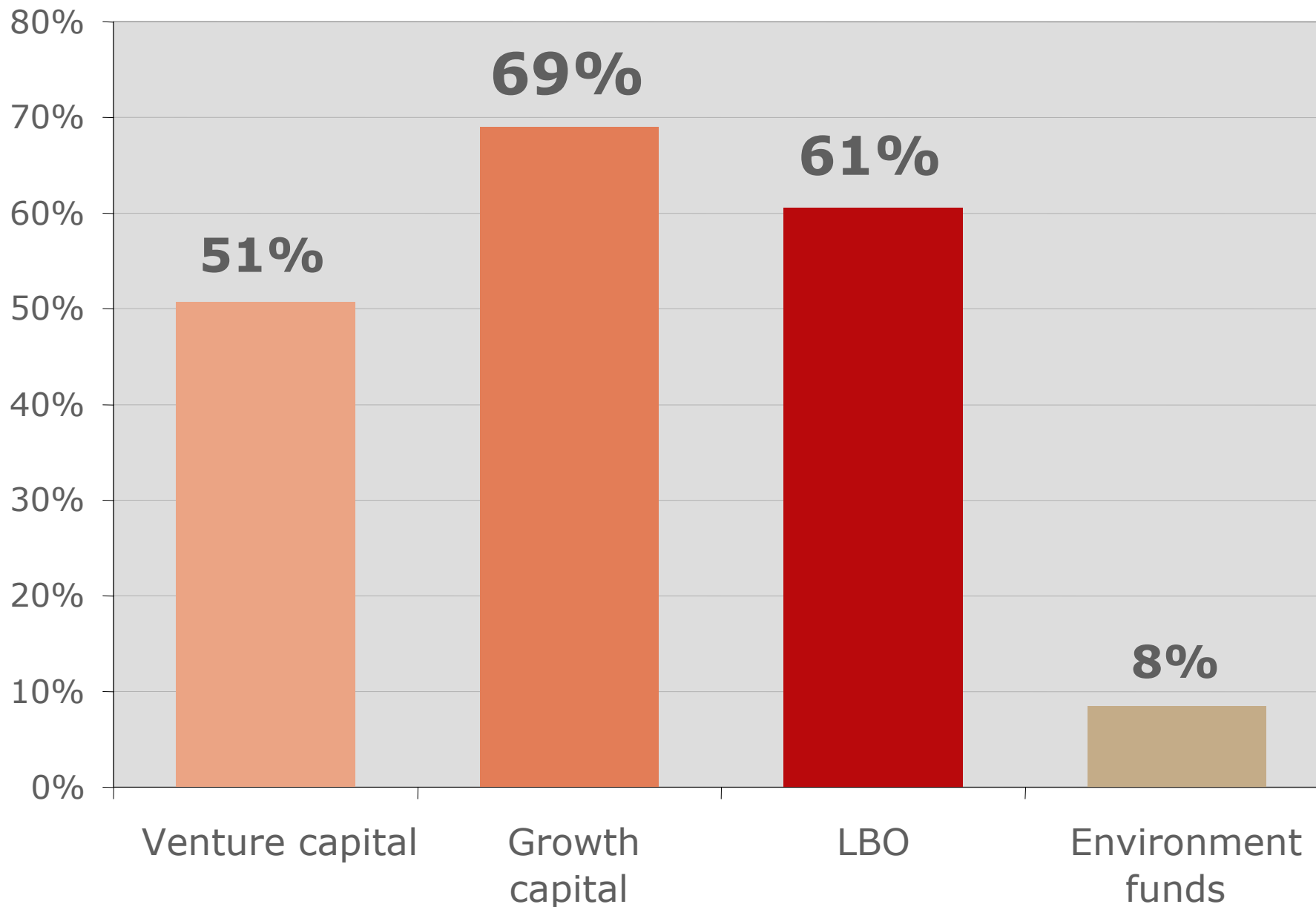
- Socially Responsible Investment (SRI) most often refers to funds that choose to invest in listed companies based on Environmental, Social and Governance (ESG) criteria. This multi-criteria analysis broadly encompasses the company's strategy and products, ranging from the economic impact of climate change on their business to human rights in high-risk countries, to the compensation of senior management or employee diversity.
- Although socially responsible private equity *per se* does not really exist, a structured approach to incorporating Environmental, Social and Governance criteria into investment choices has emerged amongst some private equity investors. As a result, this raises the questions as to, for example, the nature and standardisation of extra-financial information provided by unlisted companies and the ESG practices put in place by investors.
- Since private equity and listed companies do not have the same disclosure requirements, no specific analysis tools can be discerned as yet. However, we can begin to measure private equity managers' perception of this new investment theme, which is the purpose of this survey conducted by Novethic with the support of AXA Private Equity, in partnership with AFIC (French Private Equity Association) and France Investissement.

- A questionnaire was sent to nearly 300 French management companies that represent the private equity market in France and that are members of France Investissement and AFIC.
- 71 companies replied, i.e. **24%** of those surveyed. The high number of respondents and wide coverage of the market attest to the accuracy of the results published.
- Respondents manage regional, national and international funds.
- 5% of the panel surveyed assert that they never reply to surveys. Others declined due to time constraints.

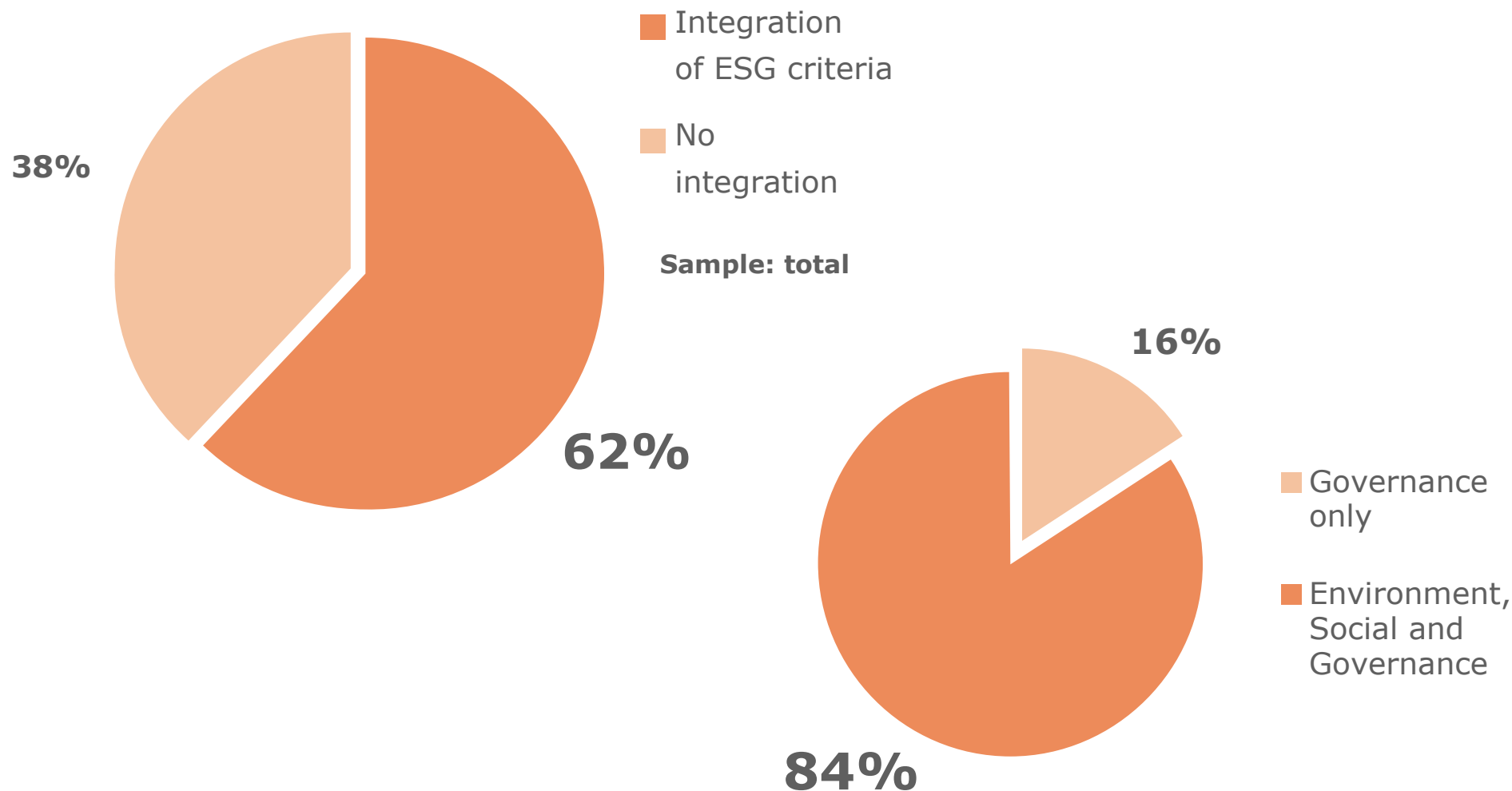
- A PLUS FINANCE
- ACTEM PARTNERS
- AGRO INVEST
- ALOE PRIVATE EQUITY SAS
- ALSACE AMORCAGE / ALSACE CREATION
- ALTO INVEST
- ALVEN CAPITAL
- AQUITAINE CREATION INVESTISSEMENT
- ARDENS ET ASSOCIES
- ARGOS SODITIC FRANCE
- ASSYA CAPITAL
- AVENIR ENTREPRISES
- AXA PRIVATE EQUITY
- BARCLAYS PRIVATE EQUITY FRANCE
- BLACKFIN CAPITAL PARTNERS
- BOURGOGNE CROISSANCE INNOVATION
- BRETAGNE JEUNES ENTREPRISES
- BTP CAPITAL INVESTISSEMENT
- CAP DECISIF
- CAPZANINE
- CARVEST
- CDC CAPITAL INVESTISSEMENT
- CDC ENTREPRISES
- CEREAL GESTION
- CHAMPAGNE-ARDENNE CROISSANCE
- CITA GESTION
- CITIZEN CAPITAL
- CLAVEL INVESTISSEMENTS
- CREAGRO
- DEMETER PARTNERS
- EDMOND DE ROTHSCHILD CAPITAL PARTNERS
- EMERTEC GESTION
- FORTIS PRIVATE EQUITY FRANCE
- FRANCHE-COMTE PME 3
- G SQUARE CAPITAL
- GREEN RECOVERY
- HERRIKOA
- ICEO
- IDEB
- IFE MEZZANINE
- INNOVACOM
- INOCAP
- INOVAM
- IRPAC
- I-SOURCE GESTION
- KOHLBERG KRAVIS ROBERTS & CO (PARIS OFFICE)
- LIMOUSIN AMORCAGE
- LMBO
- MATIGNON INVESTISSEMENT ET GESTION
- MIDI-PYRENEES CROISSANCE
- MODE ET FINANCE CONSEIL
- MONTEFIORE INVESTMENT
- NEWFUND MANAGEMENT
- ODDO ASSET MANAGEMENT
- OFI ASSET MANAGEMENT
- OFI PRIVATE EQUITY
- ORKOS CAPITAL
- PAI PARTNERS
- PHILLIMORE INVESTISSEMENT
- PICARDIE INVESTISSEMENT
- POITOU-CHARENTES EXPANSION
- SCHNEIDER ELECTRIC VENTURES
- SIGMA GESTION
- SIPAREX - SIGEFI
- SOPROMEC
- SYNERGIE FINANCE GESTION
- UI GESTION
- VATEL CAPITAL
- VENTECH
- WINDHURST
- XANGE CAPITAL



Virtually all of the firms that replied to the survey invest directly in companies. This breakdown is comparable to the private equity market, as described by AFIC. This means that investors have direct access to the ESG practices of their assets. Only two respondents invest partially or exclusively in private equity funds.



- Respondents are primarily active in the "growth capital" segment (2/3 of the management companies), followed by "LBO" (61%), while 51% are in "venture capital". This quite accurately represents the French market, despite a slight underweighting of LBO investors. The percentage provided includes both those active in only one business and those in two or three private equity businesses.
- Only 22% practice all three strategies simultaneously, substantiating the segmentation of the different private equity specialisations.
- Finally, 8% of the companies surveyed stated that they managed or invested in environment funds.



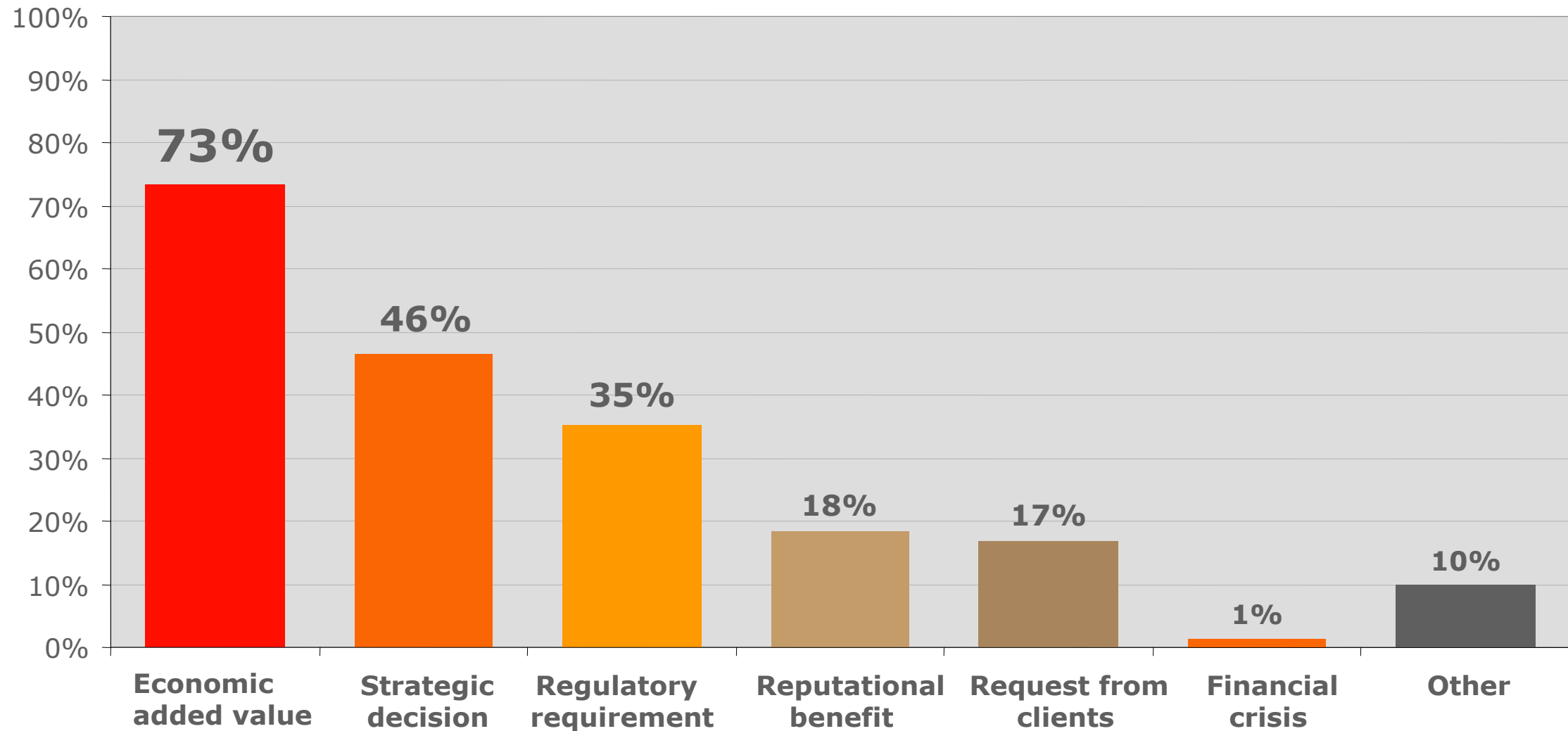
Sample: respondents with an ESG approach

Two-thirds of respondents affirm that their management company takes Environmental, Social and Governance (ESG) criteria into account in its investment decisions. The market segment breakdown illustrates that ESG criteria are integrated across the board to at least some degree. However, slightly more LBO managers (69%) report that they apply ESG criteria compared to venture capital (58%) or growth capital (56%) managers.

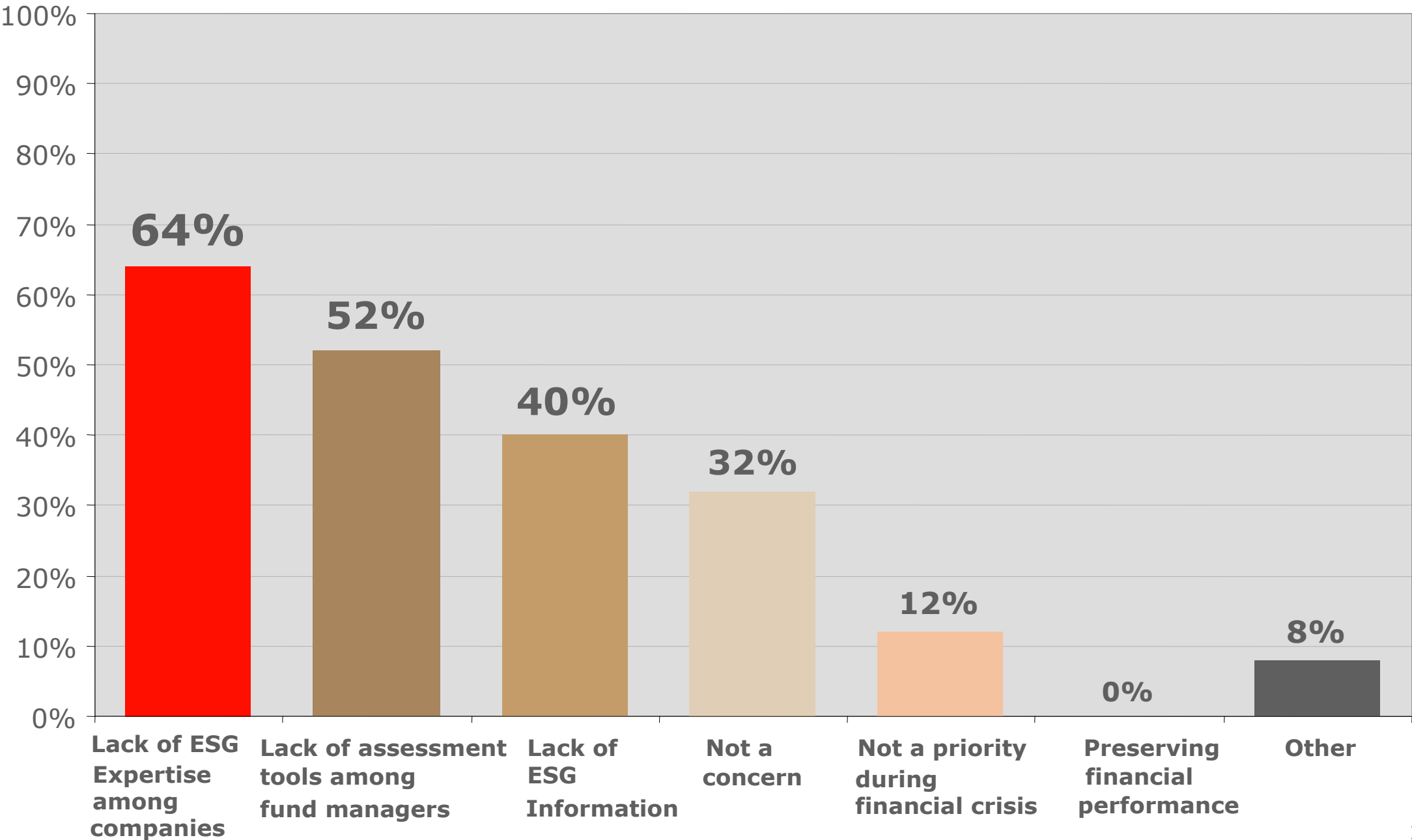
Unlike other financial sectors where the integration of ESG criteria is still nascent, the managers surveyed present a firm overall grasp of sustainable development principles.

Two cases in point:

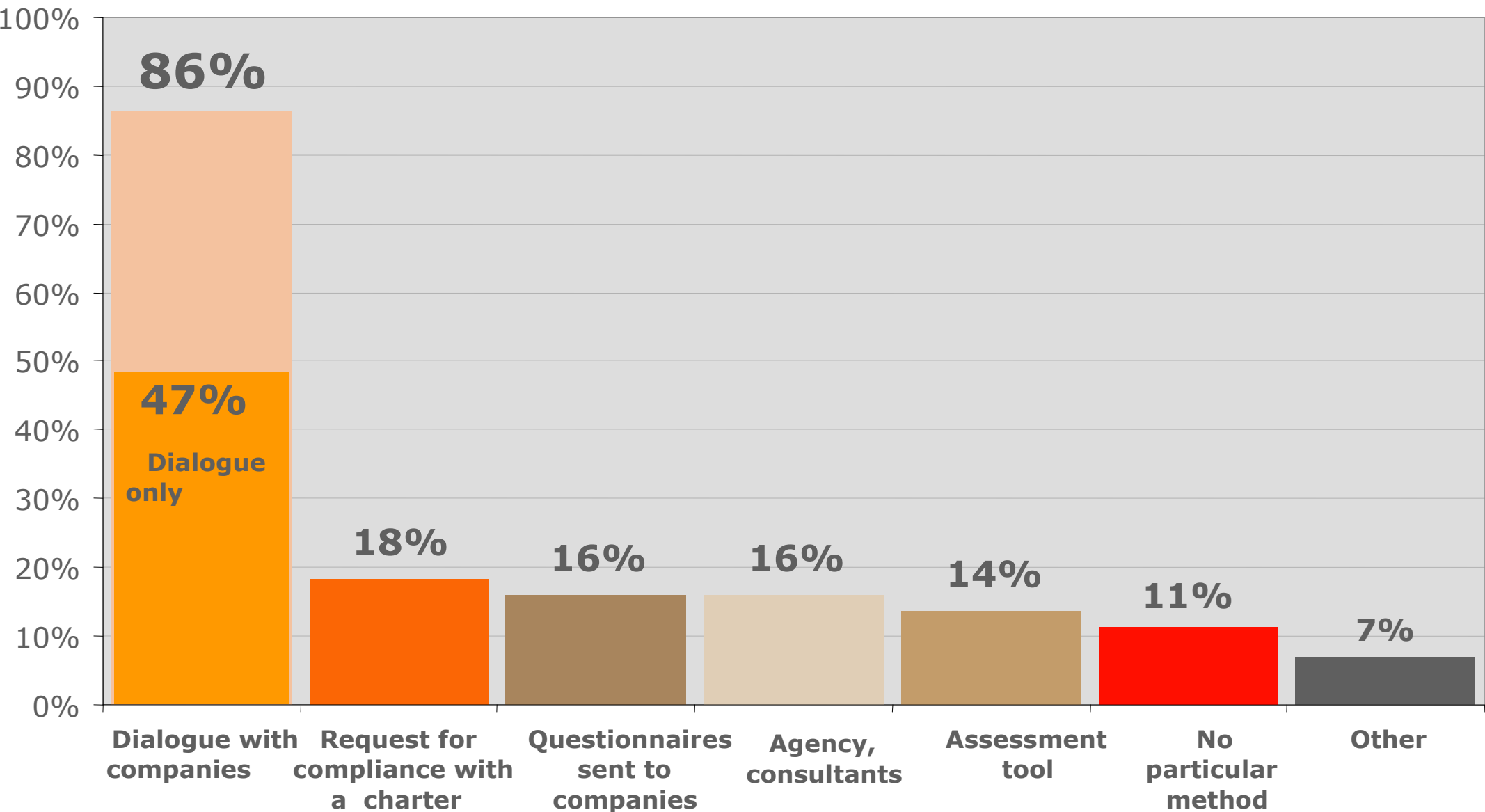
- Only 16% believe that it is limited to governance criteria.
- All managers who claim to integrate ESG criteria agree that investing in cleantech companies alone does not comply with sustainable development standards.



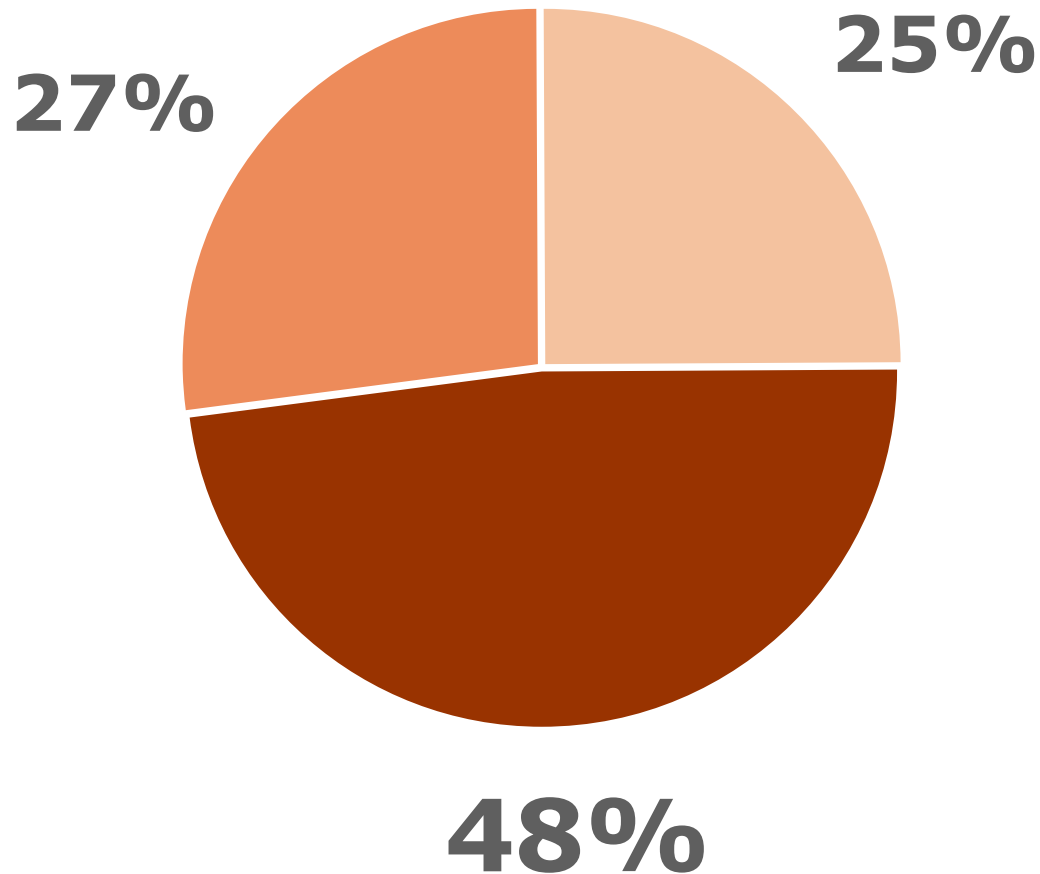
- Among the factors that encourage asset management companies to apply ESG criteria to their investment strategies, nearly three-quarters of those surveyed believe that it offers economic added value. With 46% and 35% of respondents' votes, management strategy and regulatory requirements, respectively, trail behind. Less than one out of five gave prime importance to the reputational benefit afforded by ESG criteria or a request from clients. Lastly, only one respondent believed that the financial crisis was an incentive to apply ESG criteria.
- These results show that the managers surveyed have understood how major social and environmental issues can be used in risk and opportunity management and that SRI standards are not considered a fad or a one-off opportunity. Once again, these results are quite different from those of surveys conducted a few years ago of investors that did not yet use traditional SRI strategies.
- Although regulatory requirements are considered a determining factor for management companies that do not yet apply ESG criteria (48%), they are deemed less so for companies that have willingly implemented SRI approaches (27%). However, both categories tend to agree on all other incentives.



- Among the management companies surveyed that do not apply ESG criteria, nearly two-thirds blame the lack of expertise and tools of unlisted companies. This type of approach is still in its early development phase and depends on the initiatives taken by certain players. More time is needed to build extra-financial analysis tools adapted to the differences in size and structure of unlisted companies.
- Similarly, 40% of the managers surveyed assert that the extra-financial information available from independent experts (specialised rating agencies, etc.) is inadequate to implement an ESG screening process. More than half state that they do not have in-house adapted assessment tools.
- Investors without an ESG approach do not necessarily have any financial limitations. One-third (32%) state that it is simply not a concern, especially considering that the financial crisis dissuades 12% of this group from integrating this new approach.
- However, none of the respondents think that an ESG approach would hinder their financial performance. This confirms that it is understood, from a strictly financial standpoint in both the medium and long term, more as an advantage rather than an obstacle.



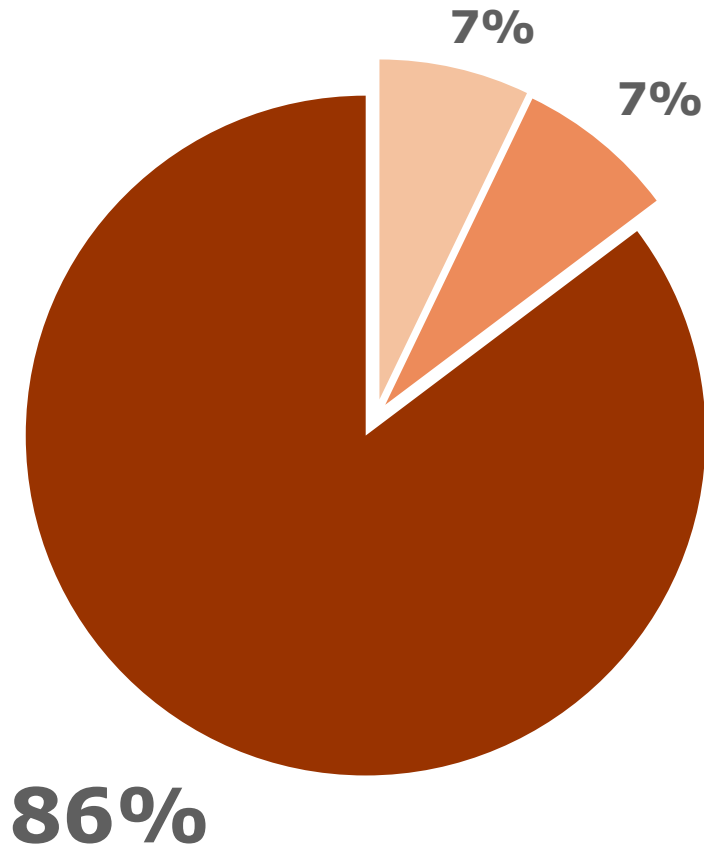
- The answers concerning investors' methods that claim to integrate ESG criteria into their investment strategy confirms that these approaches are still new. The only common technique, used by 86% of the panel of respondents, is direct dialogue with the companies in which they invest. This informal practice is difficult for third parties to assess but is largely preferred over other more formal and all-encompassing methods. No single category alone - request for compliance with a charter, questionnaires, assessment tools for companies or the use of third-party experts - came in at over 20%. Essentially, these results can no doubt be explained by the very nature of private equity businesses and the lack of a structured offer of extra-financial analysis.
- When asked what ESG integration methods are used, 11% of management companies that claim to do so apply no special methods of analysis. This may suggest more a statement of intent rather than an effort to harness economic added value.



- Management firms wishing to orient their communication on the integration of ESG criteria
- Management firms not wishing to orient their communication on the integration of ESG criteria
- No opinion

Sample: respondents with an ESG approach

- Although for some companies SRI has become their mainstay of communication and even marketing, this is hardly the case on the private equity market. Only one-quarter of the management companies that claim to integrate ESG criteria into their investment decisions express a desire to hone their communication in on this aspect. What is more, half of them do not want ESG to play a role in their communication at all.
- The fact that private equity investors do not plan to steer their communication towards this aspect of their management strategy could imply a certain degree of reluctance regarding SRI but may also simply confirm the sector's overall practice of limiting communication altogether.



- Management firms wishing to adopt an ESG approach within 1 year
- Management firms wishing to adopt an ESG approach within 2 years
- Don't know

Sample: respondents without an ESG approach

- The incorporation of ESG criteria remains within the realm of a handful of pioneers. Those who have not yet chosen to adopt these practices appear disinclined to do so. As such, it would be difficult to determine when in the near future this type of approach may become standardised. Only 14% of the management companies that state that they use no extra-financial screening process plan to adopt this type of approach within the next year or two. Conversely, 86% do not foresee the application of any ESG approach in the short to medium term.
- The lack of tools and techniques available could also explain the private equity sector's reluctance to integrate ESG criteria more systematically.

- **Private Equity** is the financial practice of investing in unlisted companies. Investors finance the companies and contribute to their development by raising quasi-capital or capital. Private equity investments average 5 to 8 years and boast higher yields than investments in stock markets (over 15% per year) but bear much greater risk. Generally speaking, private equity investors are significant or majority shareholders in the companies in which they invest, giving them a more important role in corporate governance. Active throughout all stages of company growth, private equity gears its strategies to the specific needs of each stage. It is broken down into four major segments.

- **Venture capital:** Typically, investment in technology start-ups. Venture capital investors finance companies that bear risk but promise high growth thanks to the innovative nature of their technologies, products or services. This category is sometimes broken down further: prior to venture capital is seed capital, which is used to finance the development of new technologies or products.
- **Growth capital:** Minority stake in developing a company with a firm foothold in its market and a high-growth outlook. The purpose of this type of investment is to guide the director in devising the company's development strategy in order to create value and a strong cash position in the medium term.
- **Capital transmission:** Investment in capital to finance the acquisition of an unlisted company (LBO).
- **Distressed capital:** Funding the capital of distressed companies for which measures have been identified and implemented in order to turn the company around.

Definitions: AFIC and Novethic

- **LBO (Leveraged Buyout):** Acquisition of a company by capital investors, in association with the management of the company purchased, by using varying levels of debt that will be repaid through future cash flow. This type of deal is used to take advantage of a significant leverage effect in periods of growth. There are several types of LBOs:
 - **MBO (Management Buyout):** Acquisition of a company by the management team (one or more managers, either non-shareholders or minority shareholders).
 - **MBO (Management Buyin):** Acquisition of a company by one or more managers from outside the firm.
 - **BIMBO (Buyin Management Buyout):** Acquisition of a company by a combination of a buyer from outside the firm and the seller and/or company's existing managers.
 - **OBO (Owner Buyout):** Acquisition of a company by a holding company jointly owned by the existing owner and financial investors.



Avec le soutien de :



What do private equity investors think of the integration of ESG criteria?

Survey conducted by Dominique Blanc, Samer Hobeika and Batiste Goldet from Novethic's SRI research centre and supervised by Anne-Catherine Husson-Traore, Novethic's Chief Executive.

Since 2001, Novethic provides expert resources and mobilises business leaders, investors, NGOs and other stakeholders on key topics related to CSR and SRI. Novethic is the only source of analytical and statistical information on the French SRI market. The SRI research team conducts thematic studies, analyses product trends and assesses the SRI processes of asset management firms.