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ESG Integration in the Nordic Private Equity Industry

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ACKNOWLEDGEMENTS

In this Thesis, I target ESG integration in the Nordic private equity industry. Analysing the extent of the integration and current dynamics via questionnaires and interviews, I have gained valuable insight into the beliefs and motivations of General Partners operating out of the Nordic countries. I hope to contribute to further the trends I'm uncovering in my future professional work.

I want to express sincere gratitude to my supervisor, Lars Jacob Tynes-Pedersen for his commitment to steering me on the right paths and encourage critical thinking from ideation through to the final product. Further, I would like to thank Carsten Bienz of the Argentum Centre for Private Equity at NHH for his valuable inputs on private equity, and his guidance on research objectives. Mr. Per Saxegaard, my uncle and Chairman of the Business for Peace Foundation deserves special mention. He has been a source of motivation and inspiration throughout my education, implementing in me a sense of purpose in working toward a future in which business and society walk hand in hand. Throughout my work with this thesis, he has installed in me an appreciation for private equity with all its high stake risks and opportunities. He is inspiring and challenging me continuously.

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I want to thank family and friends for encouragement during the process of writing.
I hope this thesis will be a source of inspiration –

Annik C. S. Falch

Annik Cecilie Saxegaard Falch
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ABSTRACT

After the financial crisis, the private equity industry is increasingly regulated. Macroeconomic developments are changing the business landscape, and firms are finding that they have to work harder to create returns. The private equity industry has been lagging behind when it comes to embracing sustainability, but in recent years, the industry is increasingly expected pay attention to Environmental, Social and Governance (ESG) issues in their investments.

In this thesis, I shed light on developments concerning ESG integration in private equity, an area that is scarcely researched. Narrowing my scope, I aim to give an extensive exposition of the extent of ESG integration by firms' operating out of the Nordic Countries. Research objectives are formulated on five themes, including industry insiders understanding of ESG, the extent and strategic drivers for integration, as well as organizational characteristics and future beliefs relating to ESG in private equity. I surveyed a unique set of General Partners representing 60 private equity firms headquartered in the Nordic region in 2016, and conducted interviews with five assertive firms for additional qualitative depth.

My findings show that governance issues are most important among ESG issues for Nordic GPs, and they are increasingly making efforts to measure financial impacts of ESG initiatives. Investor pressure and the possibility to create additional financial returns are reported as the main strategic drivers of ESG integration. Nordic PE is showing signs of having integrated ESG into the DNA of their operations – not just as an add-on activity in their investments. They are moving beyond a compliance- and value *protecting* attitude toward ESG management, and are applying it as a value *creating* strategy and a means for obtaining competitive advantage. Furthermore, my findings indicate that a company culture embracing ESG and the adoption of an "ESG mindset" is important for successfully extracting added value from ESG efforts. Finally, I find that PE show signs of acknowledging their role as active managers in creating the sustainable companies of the future.

By researching the Nordic area, often perceived as a forerunner on sustainability, I am able to map cutting edge industry developments. Thus, my thesis is a contribution to the emerging field of research on ESG integration in the private equity industry, and particularly opens up for further research on the financial rationales for pursuing ESG. With this research, I will give a comprehensive exposition of the state of affairs and trends on the integration of ESG issues in the Nordic private equity industry. Further, my work will provide private equity agents with insights into the strategic rationales for pursuing ESG as well as knowledge on the activities of their peers.

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KEY WORDS

Private Equity, Socially Responsible Investment, ESG, UN SDGs

TERMINOLOGY

PE: Private Equity

GPs: General Partners

LPs: Limited Partners

ESG Environmental, Social and Governance

SRI: Socially Responsible Investment

KPIs: Key Performance Indicators

NGOs: Non-Governmental Organizations

There is only so much a few people can do, and if we want this to move at scale, it needs to be part of people's everyday work. Society, the financial industry, the private equity industry, EQT – we are all on a journey. We need to learn to speak the same language, see the opportunities the sustainability agenda brings and continue to push for positive change.

- EQT

1. INTRODUCTION

Going forward, our societies and the environment will face increasing pressures. Climate changes, population growth and urbanization, growing economic inequalities and government fiscal strains characterize a world that is becoming increasingly more technologically interconnected. It is not controversial to put blame on the business society for negative developments due to environmental ignorance, poor product quality and safety, and questionable business conduct. Increasingly, business is being held responsible for its actions. Socially Responsible operations are demanded of corporations, and lately, sustainability concerns have also appeared on the agenda in the financial industry.

In the private equity industry however, changes have been a long time coming. The industry has long been standing on the sidelines with General Partners having excused their investors for only caring about high returns on their investments, or voiced that the increased transparency demands or non-financial aims that comes with socially responsible investments goes against their fiduciary duties (UNPRI, 2015). Over the last decades, this general attitude has played a part in giving the industry a reputation for prioritizing employee and investor dividends over portfolio company viability.

Recently, we have seen developments within private equity. Where before credible ESG data were only available for public markets though firms and companies such as *Bloomberg*, *MSCI* and *Sustainalytics*, today technological developments are allowing credible collection of ESG data related to private equity. Agents, such as private equity funds of funds managers *Robeco* and *Adveq* are supplying markets with data on ESG impacts, and the UNPRI (United Nations Principles for Responsible Investment) continues to build competence and spread information on responsible investing as their signatory base increases (Weide, 2016). Investors are thus increasingly informed on companies' non-financial performance. Evidence shows that investors see the connection between effective management of Environmental, Social and Governance (ESG) issues and the long term successes of their investments, and are raising the bar on ESG integration for PE firms. UNPRI (2014) defines ESG integration as having processes in place for identification, management and reporting on ESG risks and opportunities in investment decisions and monitoring activities.

Notably, evidence on ESG activities have increasingly become a requisite for investors to partake in fundraising (PwC, 2015). The idea that investors as "shareholders" simply want to maximize profits is no longer the rule. Within the organizations, changes are also seen in the field of human resources. The increased interconnection of finance and sustainability require employees mastering different skill sets, both in terms of technological expertize and knowledge on ESG and sustainability. Moreover, the millennium generation is making its way into the industry, and with them a greater need for purpose and fulfilment (More, 2014).

The potential advantages to ESG integration inherent in private equity operations, indicate that the industry could become a important player when it comes to ESG integration. Private equity firms take ownership over private companies, the backbone of our economies (Crifo, Forget & Teyssier, 2015). With the firm's active engagement in portfolio company management and long investments horizons, coupled with an opportunity driven mind-set among its employees (UNPRI, 2014), they are not only laying the groundwork for successful exits, they are also influencing the kinds of companies that are going to define our future (Koch, 2016).

Until now however, most literature on Sustainability and ESG has focused whether such orientation has led to superior financial performance for companies or asset managers investing in listed firms. This has more often than not concluded with a correlation between ESG efforts and both financial and social results (see for example Eccles, Ioannou and Serafeim, 2014). The literature is slim however on both the strategic and financial rationales for private equity firms integrating ESG into their organization and investments. I my thesis I want to address this knowledge gap, and look into the value creation potential of PE companies' ESG integration.

To examine industry dynamics, I have chosen to target Nordic countries, commonly viewed as forerunners on sustainability (Karlsson & Alers, 2013). My main research objective is thus to investigate Nordic private equity firm's integration of ESG in their investments and operations. My aim is to provide investment professionals and the overall private equity industry with an overview of industry best practices when it comes to pursuing ESG and sustainability. The main research objective is further operationalized to reflect important dynamics, and includes looking into current understanding and degree of ESG integration, motivations for pursuing an ESG strategy, performance metrics, changes in company operations with respect to views on value creation and company culture, and significant future trajectories. Detailed research questions of the study are outlined in chapter 2.2 and 2.3.

To make the case, I will begin by synthesizing existing literature and emerging trends. Further, I will tap into the beliefs and attitudes of General Partners. Mainly, this investigation is conducted in the form of a quantitative survey of private equity firm's in the Nordic countries, singled out via the Preqin Database on private equity and filtering for fund managers headquartered in the Nordic region. Additionally, I will conduct semi-structured interviews with assertive firms to supply my findings with additional qualitative depth.

With this research, I will give a comprehensive exposition of the state of affairs and cutting edge trends on the integration of ESG issues in the Nordic private equity industry. I problematize the industry's future license to operate in a world where business operations are being increasingly scrutinized. My work will provide private equity agents with insights on the value creating potential of sustainable operations and knowledge on the activities of their peers.

This study opens up for further research addressing the financial value creating potential of socially responsible investment and ESG integration by going deeper into empirical findings on financial results. Further, interesting areas of research include differences in ESG integration between asset classes, as well as the value creation potential due to employee motivation with regards to ESG. (See chapter 6.3. for additional future research suggestions).

1.1. SCOPE AND DELIMITATIONS

To introduce readers to the detailed research questions, I will begin by giving an account of private equity and the Nordic countries. (chapter 2.1) In chapter 2.2. I will direct my focus towards ESG and SRI. I will define the terms, give an account for the development of the concepts and look into frameworks and findings on the prevalence of ESG activities in private equity industry today. Logically related to these aspects, I will present research questions 1 and 2. In chapter 2.3, I will synthesize literature related to strategic ESG drivers and obstacles, organizational characteristic related to ESG integration and future indications. Following, I will pose research questions 3, 4 and 5. In chapter 3, I will account for the methodological choices defining the thesis, and guide the reader through the development and execution of the literature review, online survey and semi-structured interviews that provided me with an understanding of the context and data to answer my research questions. In chapter 4, I will lead the reader through particular findings from the survey (providing insights on all research areas) and from the interviews (supplying depth to the questions problematizing motivations, organizational characteristics and future beliefs). In chapter 5, I will draw on the findings and engage in a discussion on the significance of ESG, putting weight on aspects relevant to private equity firm's going forward. Lastly, I will conclude, look into implications for industry agents and theoretical frameworks, comment on limitations of my research and point to directions for future research.

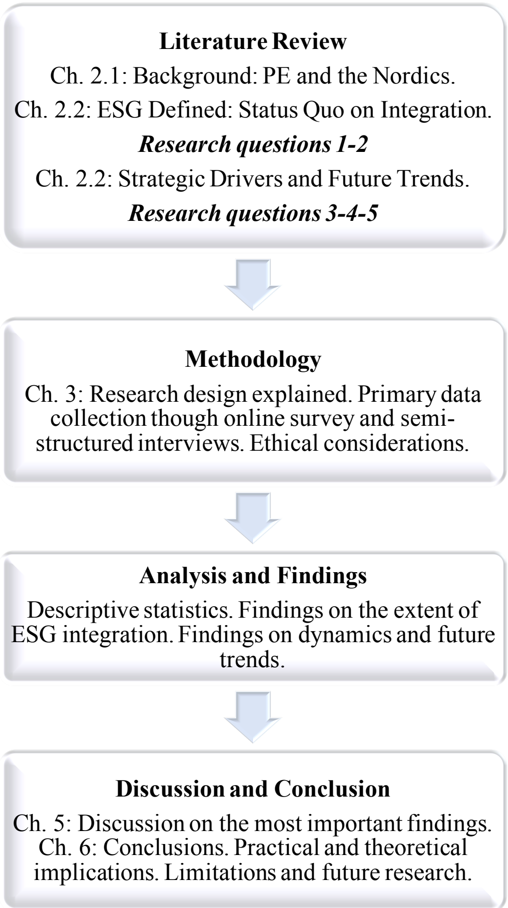


Figure 1: Outline of the thesis

I limit my research to problematize ESG within the scope of the *Nordic* private equity industry. (Characteristics of the countries and the industry are found in chapter 2.1.). Importantly, I will look at the characteristics from a *strategic perspective*, probing into diverse private equity firms' appreciations for ESG and the rationales for their operational choices. This approach reflects that the thesis is written as finalizing part of my Master's degree in Strategy and Management. As the primary aim for the private equity industry is creating returns however (as explicitly argued for by the interview participants, see appendix 8.3), I will highlight various arguments for ESG integration from a financial perspective. The summary found in chapter 2.2.2. *Business case of ESG*, display different findings on the value creating potential of ESG integration. Among the drivers for integration found in chapter 2.3.2. *Drivers of ESG & SRI in PE*, possibilities for obtaining financial results from ESG integration is illuminated. Answering the research questions, I enquire about evidence on value creation (both in the survey and in the interviews), and findings on these accounts are more closely described in chapter 4. *Analysis and Findings*, and chapter 5.1. *Discussion on the findings*. Valuable directions for further research posed in chapter 5.3. *Research Limitations and Suggestions for Further Research* include looking into ESG integration in private equity from a financial perspective, empirically examining how ESG measures affect fund performance expressed as ROI, ROA, IRR, valuations and so on. While my research examines different strategies regarding financial returns, I regret not having the time to do additional financial analyses in this thesis.

2. THEORETICAL FRAMEWORKS AND RESEARCH QUESTIONS

In this chapter, I will synthesize emergent literature and thus provide context for answering my research questions. In chapter 2.1: *Background: About Private Equity and the Nordic Countries,* I will start by providing background information on the characteristics of the private equity industry, including the extent and development. Following, I will turn my focus toward the Nordic countries, giving a general account of country characteristics, as well as an overview of the private equity industry in the area. Next, I will look at ESG integration through a theoretical lens. Having first established this general frame, in chapter 2.2: *ESG Defined: Status Quo on Integration,* I turn towards ESG. I will define and present the development of the concepts of ESG and SRI, and look into notable frameworks and tools aiding the integration of ESG into private equity. Finally, I will summarize findings on the characteristics and extent of ESG integration in the Nordics, with weight on the "materiality approach" in measuring impacts of ESG. Based on these aspects, I will present research questions 1 and 2, aiming to map private equity firm's understanding of ESG, and the extent of ESG integration (strategies and procedures adopted) in the Nordic countries. In chapter 2.3: *Findings on Industry Dynamics and Future Trajectories*, I will go deeper into the literature and portray cutting edge insights on the dynamics and trends characterizing the industry. Problematizing motivations and barriers to ESG integration, I will present findings on drivers internal and external to the private equity companies, as well as common obstacles voiced by firms. Changes in organizational characteristics related to ESG management is presented, and I will summarize pointers to important future trends. On these grounds, I will present research questions 3, 4 and 5, problematizing private equity firms' strategic rationales for engaging in ESG management, developments within company operations related to ESG, and the role the private equity industry will have in our societies going forward.

2.1 BACKGROUND: ABOUT PRIVATE EQUITY AND THE NORDIC COUNTRIES

2.1.1. ABOUT PRIVATE EQUITY

The private equity industry is an important player in our economies, as it finances private companies and foster new and innovative companies. Private equity firms ("General Partners"), are provided working capital from investors ("Limited Partners"). This capital is directed into private equity funds, which then again is used to buy private companies, or public companies with the intention of taking them private. The companies are usually held for 4-7 years. When the companies are exited, returned capital is distributed to Limited and General Partners. General Partners are also paid annual "Management fees" by the Limited partners for operating the investments.

Private equity asset classes. *Source: Invest Europe, 2016.*	
Buyout	Targeting mature industries and acquiring controlling stakes in companies already established.
Venture Capital	Usually making minority investments in young and often innovative companies in need of capital for research and development
Growth Capital	Usually making minority investments in relatively mature companies that are looking for capital to expand or restructure operations or enter new markets.
Turnaround/ Rescue	Making minority investments in existing businesses experiencing trading difficulties, aiming at re-establishing prosperity.
Mezzanine	Providing debt to companies, with the rights to ownership or equity interest in case of default, after other lenders (such as Venture capitalists) are paid.
Secondaries/ Replacement	Acquisition of minority stakes in a company from other private equity investors or shareholders.
Funds of funds	Private equity investments in funds belonging to other private equity investors.

Table 1: Overview of prevalent private equity asset classes

Invest Europe (2016) assesses the most prominent limited partners in Europe to be pension funds, sovereign wealth funds, funds of funds, government agencies and banks. Moreover, the most common exit strategies in Europe is trade sales (sale of company shares to industrial investors), sales to another private equity firm, and public offerings (sale or distribution of a company's shares to the public for the first time by listing the company on the stock exchange). Limited partners are the legal owners of the assets, and while they do not manage the assets invested in private equity firms, they assess the quality of the investments made by the private equity firms on a regular basis (Blackrock, 2014 and Crifo & Forget, 2012). See table 1 for an explanation of the most prevalent asset classes within private equity.

2.1.2. DEVELOPMENT OF PRIVATE EQUITY

The 1980's were a golden age for the private equity industry. The firms thrived in markets where Leveraged Buyouts (LBOs) and junk bond financing were common. Leveraged Buyouts, compared to the Buyouts we see today, is acquisitions of companies financed with a smaller portion of equity and a substantial portion of debt. In the 1990's when the junk bond market crashed, the PE industry did almost disappear (Kaplan and Strömberg 2009), and many of the companies they owned defaulted or went bankrupt due to the massive amounts of debt built up on their behalf by the PE companies. These events established the sour reputation the industry has dealt with since.

The industry did however survive through the crash, and grew steadily to become an important financial body once again as we entered into the new millennium. The industry thrived under the euphoric credit markets advancing the financial crisis of 2008 (Kaplan and Strömberg 2009). In the financial crisis however, PE companies suffered greatly along with the rest of economy, particularly because fundraising and debt markets plummeted (Crifo & Forget, 2012).

After the crisis, the macro economy improved, and the asset value of the portfolio companies bought by private equity firms immediately before and during the crisis increased. This development is reflected by 2013 and 2014 being the strongest years on record when it comes to sales of companies owned by private equity firms. Investors got their money back on a large scale, and many reinvested large sums in private equity. Private equity firms, now with the opportunity to compete for lucrative deals, increased their bids (Malk, 2015). According to Pitchbook 1Q 2015 Private Equity Deal Multiples and Trends Report, the average EBITDA multiples increased from 6x to almost 8x between 2012 and 2014.

These developments initiated operational changes in private equity firms. The high deal prices made successful returns due to changes in beta alone less likely, with beta referring to passive returns based on elements such as overall GDP growth, multiple increase and leverage, as opposed to return due to active management (Malk, 2015). Returns on investments today are closely related to GPs ability to protect and create value (UNPRI, 2014), and GPs are engaging actively in portfolio company operations to generate returns. This is done by targeting underperforming firms and accelerating their growth, instead of trusting the financial leverage effect (Boucly et al. 2009). Closely related is a more thorough Due Diligence process in investment decisions, ensuring that their investment can *withstand any economic or market climate*" (Bain & Company, 2015).

As the industry is again gaining foothold however, the rules of the game has changed. Recognizing that the way the financial markets operated before the financial crisis were not sustainable, national and international bodies have imposed strict regulations on the financial industry as a whole. Notably, president Obama signed the Dodd Frank Act in 2010. In Europe, The European Union passed the Alternative Investment Fund Managers Directive (AIFMD) in 2011, regulating private equity and other Alternative Investment Fund Managers. Such initiatives are requiring private equity companies to act transparently and report on their operations, and puts risk management on the agenda (Talmor & Vasvari, 2014).

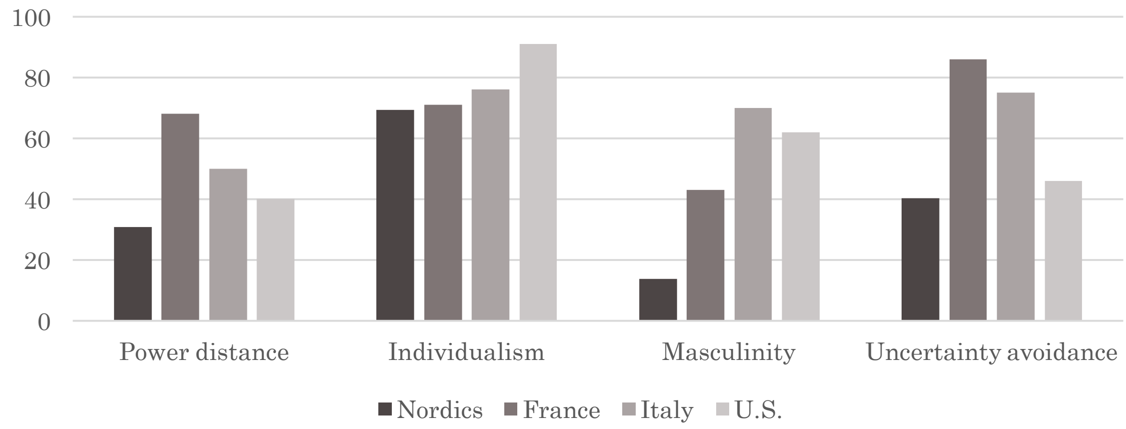
2.1.3. CHARACTERISTICS OF THE NORDIC COUNTRIES

The Nordic countries comprises of Denmark, Finland, Iceland, Norway, Sweden, Iceland and Greenland (an autonomous country within the Danish Realm). Politically, Sweden, Denmark and Finland are part of the EU, with Finland being the only country using the Euro. Iceland applied for EU membership in 2009 after its banking system was severely impacted by the financial crisis, but have since dropped its bid. During the financial crisis, the Nordic area were less impacted, due facts such as Finland being the only country using the Euro, and that the countries having experienced local financial crises in the 80s and 90s. This provided the countries with knowledge to put their economies in order (BerchWood, 2013). Iceland however, were hit hard in 2008, when three of its biggest banks defaulted and left the country in severe debt.

Standard & Poor's credit rankings for the Nordic countries are high, with Sweden, Denmark and Norway being rated AAA, and Finland AA+. During and after the financial crisis, the amount of investments has been stable. Iceland no longer holds a BB+, but is rated at a BBB+ with a stable outlook. In the global competitiveness index (the World Economic forum), as well as the ranking of countries where it is easiest to start and run a business (the World Bank and the International Finance Corporation), Finland, Sweden, Denmark and Norway all appear among the top 15. OECDs Real GDP Forecast expect strong economic growth in both 2016 and 2017 for all of the Nordic countries (OECD, 2016).

The Nordic countries are characterized by welfare systems based on high taxation, extensive public service and high levels of social security (Spliid, 2013). Moreover, they are described as having cultures fostering innovation and entrepreneurship, valuing transparency, having open economies and being ahead on education and technological adoption (BerchWood, 2013). According to RobecoSAM research, Nordic countries are more sustainable, egalitarian and are making more social progress than most other countries. Nordic companies are leading the way in terms of sustainability, especially when it comes to reporting and supply chain management. (Karlsson & Alers, 2013).

From a theoretical perspective, the Nordic countries show similarities on several cultural dimensions (Hofstede, 1980; 2010). Looking at Denmark, Finland, Sweden and Norway, the countries are characterized as feminine and collectively oriented. Feminine values include relationships and the quality of life, whereas earnings, recognition and advancement are viewed as masculine. Collectivism deals with loyalty, integration and conclusion, contrasting individualism and loose personal ties. The Nordics have low power distance, defined by low acceptance of inequalities and the treatment of others as equals, and they score relatively low on uncertainty avoidance, meaning that they are not threatened by unknown situations. To illustrate contrasts, the US scores higher on individualism and masculinity, and countries such as France and Italy score higher power distance and uncertainty avoidance.



Source: Hofstede, 1980; 2010. Mean scores applied for Denmark, Finland, Norway and Sweden.

2.1.4. THE NORDIC PRIVATE EQUITY INDUSTRY

In his 2013 article on the characteristics of Nordic private equity, Robert Spliid finds that in comparison to private equity in the US, the Nordic private equity markets are less developed. Fundraising is more difficult due to investors representing a diverse group of jurisdictions, credit sources are fewer as the credit markets are bank-dominated and governments are more keen on controlling financial markets and reduce PE's tax advantages.

According to Preqin there are 283 private equity firms based in the Nordic region, comprising all of the major types such as buyout, growth, venture, mezzanine, turnaround, secondaries and funds of funds. This number tells of a significant increase in firms operating from the Nordic region, as there were only 197 in July 2013 (preqin.com). Out of the 283, Sweden accounts for the biggest portion, with 109 firms (39%). Following are Finland with 62 firms (22%), Denmark with 50 (18%), Norway with 49 (17%), Iceland with 12 (4%) and Greenland with 1 company. In relative terms, Invest Europe have estimated that Nordic PE companies (Excluding Iceland and Greenland) constitutes 14% the European total (Invest Europe, 2013). The largest firms of the area include Swedish EQT, Nordic Capital and Altor, Finnish CapMan, Danish Axcel and ATP PEP, and Norwegian Norvestor Equity and HitecVision. Greenland Ventures is the only company operating out of Greenland.

In 2015, fund managers operating out of the region (excluding Iceland) raised €7.8bn, just above 16% of the €47,6bn European total of funds raised. Investors in Nordic funds are dominated by pension funds (21%), and sovereign wealth funds (21%), followed by funds of funds & other asset managers (15%), government agencies (13%) and banks (10%) (Invest Europe, 2016). According to Argentum (2015), Nordic investments totalled approximately €6,3bn, including, 110 buyout investments (€5.8bn) and 233 venture investments (€497mn). In comparison, Invest Europe calculated the European total to be €47,4bn in 2015. The S&P Global Market Intelligence Report shows that Sweden ranks first in terms of invested capital, with Norway and Denmark following. The report also state that IT was the sector most invested in by private equity in the Nordics in 2015, and was also the sector with the highest number of new deals between 2011- 2015. Cross-border investments within the region is perceived as less risky for Nordic investors, due to their strong language and cultural ties (Spliid, 2013).

White and Case, a global law firm based in Stockholm, interviewed top investment professionals from leading Swedish PE firms in early 2016. The professionals believed that the Nordic private equity industry is likely to continue the trend of positive performance seen in recent years, with 2016 meeting or exceed 2015 performance (Johansson, Pettersson & Wireklint, 2016).

2.1.5. A THEORETICAL ACCOUNT OF PRIVATE EQUITY AND ESG

From a theoretical viewpoint on Private Equity, what may explain that ESG considerations have appeared on firms' agenda? As a backdrop, private equity can be accounted for through the principal-agent theory, which is well recognized in economics literature. The theory is about a relationship in the form of a contract, where a principal (or principals) engages an agent to perform a service on their behalf, involving transfer of some decision-making authority from the principal to the agent (Jensen & Meckling, 1976). Theoretically, private equity is viewed as a form of asset management where the General Partners ("agents") effectively maximizes value for shareholders (investors, the "principals"), characterized by minimization of agency costs and effectively incentivising private equity professionals by applying performance based compensation schemes (Jensen, 1986). The principal-agent theory is grounded on financial incentives being the main motivational factor for the agents. In light of this, considerations of ESG seems to be in conflict with the theory, as it would seem to imply spending financial resources on providing public good (Crifo & Forget, 2012). As noted in chapter 2.1.2. Development of Private Equity, past characteristics of private equity arguably reflect this general attitude, as the industry provided investors with high returns, with little regards to what can be viewed as ESG concerns.

In his publication on international cultural differences, Geert Hofstede found that principal-agent theory assumptions such as the contractual relationship and motivation, is bound by national boundaries (Hofstede, 2010). The agency theory based on financial incentives, (which can be said to constitute a more masculine ideal), may not fare well within the Nordic countries. Robert Spliid argues for this view when he compares private equity in the Nordic countries (excluding Iceland) with the US and concludes that the financial incentives may not have the same effect with Nordic managers than with those in the US, where the culture is more masculine. (For his assertions on the Nordic countries, see 2.1.3.) Mind, Spliid encourages further empirical testing on Nordic PE managers with regards to the principal agent theory.

Researchers Dirk Matten and Jeremy Moon goes deeper into the ideas that country characteristics, in the form of historically grown institutional frameworks, can explain national differences in Corporate Social Responsibility. (Matten and Moon, 2008). Talking of CSR as an idea reflecting the social imperatives and consequences in relation to business successes, their article can also illuminate characteristics applicable for the Private Equity industry. The authors examine institutional frameworks such as the political system, the financial system, the education and labour system and the cultural system and argue for example that CSR in such "National business systems" differ among countries.

2.2. ESG DEFINED: STATUS QUO ON INTEGRATION

2.2.1. THE CONCEPTS OF ESG & SOCIALLY RESPONSIBLE INVESTING

Environmental, Social and Governance (ESG) related to investments is referring to the three central non-financial factors in measuring impact. Within the criteria lies numerous considerations related to environmental stewardship, social equity, and corporate governance, where the goal is to protect and create value (Malk, 2015). Findings from INSEAD (2014) conclude that private equity firms primarily focus on improving eco-efficiency and developing environmentally sustainable products and services when it comes to the environmental factors. They manage developmental impact, labour, health and safety factors affecting portfolio companies when it comes to social factors. Finally, they ensure robust governance structures and work on anti-bribery and anti-corruption when it comes to governance factors. Research done on the relative importance GPs assign the different pillars, show that there is more focus on governance issues (PwC, 2015). PwC's reasoning for this finding includes that the link between governance issues and value is more clearly understood by investors, which again influences GPs. This finding mirrors the same research undergone in 2015, finding that 86% of firms monitor governance issues in their investments, 80% monitor environmental issues and 76% social issues (PwC, 2013). According to the most recent report on Principles for Responsible Investment, ESG issues can affect the financial performance of investment portfolios, but to varying degrees across companies, sectors, regions, asset classes and through time (UNPRI, 2016a).

Socially Responsible Investing (SRI) is often used interchangeably with "Sustainable and Responsible Investing" or termed Responsible Investing (RI). SRI is focused on the integration of ESG risks and opportunities in the investment process with the aim of generating long-term competitive financial returns and positive societal impact. While acknowledging that there exists a great deal of different definitions of SRI, in their 2016 report, Eurosif gives an attempt at defining the concept. *"Sustainable and Responsible Investment ("SRI") is a long-term oriented investment approach, which integrates ESG factors in the research, analysis and selection process of securities within an investment portfolio. It combines fundamental analysis and engagement with an evaluation of ESG factors in order to better* *capture long term returns for investors, and to benefit society by influencing the behaviour of companies."* (Eurosif, 2016). Different labels for SRI investments include ethical, green, socially responsible, sustainable, community-based, triple- bottom line-focused, impact-focused, mission-related or value-based investments. Socially Responsible Investments correspond to multiple strategies, including exclusion, norms-based screening, best-in-class (positive) investment selection, sustainability themes investment, ESG integration, engagement and impact investing (Eurosif, 2016). To give a picture of the extent of SRI, Eurosif provides annual reports on the extent and development of SRI in Europe. Their 2016 report cover SRI practices and trends, based on findings from 13 European countries (Eurosif, 2016). Most important findings include exclusion being the most prominent strategy, followed by norms-based screening. Impact investing is the fastest growing strategy however, with sustainability themed investing following.

In the literature on private equity, the term "responsible investment" is often used synonymous to "ESG integration", and for the purposes of my thesis, I will use the concepts of SRI and ESG interchangeably. While the names differ, the meaning remains the same, namely a focus on both financial and sustainable value creation.

2.2.3. FRAMEWORKS

A number of different frameworks for integrating ESG have emerged over the last years, as well as toolkits and resources to help GPs in activities such as integrating ESG clauses into investment agreements, monitoring portfolio companies, measuring financial impacts of ESG performance and developing procedures for reporting.

In 2009 the private equity industry made a large step forward concerning SRI and ESG integration, with the launch of the United Nations Principles for Responsible Investing (UNPRI). UNPRI aims to support its signatory base of investors in incorporating ESG factors into their investment and ownership decisions (unpri.org). UNPRI has now grown to include over 1500 signatories from all over the world, representing over $60tn in assets. Almost 800 of these signatories have investments in private equity. In the Nordic area, Signatories to the UN PRI include Swedish Segulah, Alder and Priveq Investment, Norwegian DNB (Private Equity), Investinor and FSN Capital and Danish Axcel, Maj Invest and Vaekstfonden.

The UN Global Compact encourages CEOs from around the world to commit to implement universal sustainability principles and to report on their implementation (unglobalcompact.org). Among its over 9000 company participants, Nordic private equity participants include Swedish Swedfund International, Industrivärden, Investor AB Ratos and Kinnevik, Norwegian Investinor and Argentum and Danish Axcel.

Invest Europe's Investor Reporting Guidelines (formerly EVCA Investor Reporting Guidelines) is another commonly used framework by European private equity investors. The guidelines showcases principles for ethical behaviour between investors, GPs and portfolio companies (investeurope.eu).

Frameworks and guidelines put forward by national industry associations are largely applied by Nordic GPs. Major regional private equity and venture capital associations across in the Nordic region include DVCA (Denmark), FVCA (Finland), NVCA (Norway) and SVCA (Sweden).

Additional noteworthy frameworks and guidelines include PEGCC Guidelines, ESG Disclosure Framework for Private Equity, IFC Performance Standards, CDP's global disclosure system, CDC Toolkit for Fund Managers, IFC's Sustainability Performance Standards and GRI's Sustainability Reporting Framework.

All of these frameworks and guidelines are aiming to ensure that the way financial markets operate is securing stable growth, and simultaneously benefiting society. An important development on a global scale, arguably summing up what such initiatives ultimately pursue, is the United Nations SDGs of 2015. Governments all over the world have come together and commanded the business society as a whole to join the ranks working toward a sustainable future, to *"end poverty, protect the planet, and ensure prosperity for all"* (un.org). While these goals do not serve as a framework for integrating ESG issues into company operations per se, initiatives are popping up aiming at aligning business operation and the different goals. As an example, the latest guide from UNPRI present a case study on how investors can forecast the future value of listed equities by assessing how trends related to the different SDGs might impact their investments (UNPRI, 2016a).

2.2.4. THE PREVALENCE OF ESG ACTIVITIES

Findings from the UNPRI Report on Progress: Private Equity, show that it is within Growth Capital and Buyouts that ESG performance is at its best, given that the firms manage more than 50% of the assets in their portfolio companies. This, they claim, is because smaller venture capital investments are often incompatible with formal ESG implementation activities such as developing ESG policies, setting objectives and establishing reporting systems. The buyout segment account for most investments. (In comparison, €5,8bn were invested by buyout funds and €497mn by venture funds in the Nordic area in 2015.) However, the venture capital segment, with its preference for investing in innovative environmental technologies and at the same time creating jobs from scratch and instilling new and effective governance processes, is also in an especially advantageous position for effective ESG impact. (UNPRI, 2016b)

The UNPRI report (2016b) further illuminate the prevalence buyout has over venture capital by stating that private equity firms show lower ESG performances when they hold minority stakes in their portfolio companies (which venture capital does), as this limits their abilities to influence portfolio company decisions. However, as ERM pointed out in a 2016 survey of GPs and LPs, companies with minority stakes can still influence their investments by conducting thorough ESG Due Diligence, and thereby early address important ESG risks and opportunities (ERM, 2016).

When it comes to ESG integration in the different stages of the investment process, a 2015 report by London Business School and the Coller Institute of Private Equity surveyed GPs to understand the role ESG plays in private equity value creation (Ioannou, Cornelli & Zhang, 2015). Examining how companies consider ESG matters in investment decisions, during ownership or in preparing for exit, they found that firms are twice as likely to address ESG in the *investment decision* and *ownership* stage (22 respondents each) than in the *exit* stage (11 respondents). These findings they claim, suggest that ESG is important in evaluation of prospective investments and in fund manager selection, as well as being an important path to value creation. The lower score on the exit-stage, suggests that ESG is not a mere window-dressing when portfolio companies are prepared for sale.

Placement of ESG responsibilities within private equity firms vary. The earlier mentioned report by London Business School found that the likelihood of ESG policies being set and enforced are higher the higher up in the organization responsibilities are assigned. An important takeaway from this article is that for the largest firms surveyed, ESG *policy setting* were commonly set at the board level, suggesting that ESG is securing its place among the topics discussed at the highest levels of decision-making. When it comes to ESG *implementation*, LBS found that responsibilities primarily fell upon with investment professionals. Some firms had designated ESG staff, but only a smaller part of respondents reported that the responsibilities fell onto Compliance Officers or Investor Relations Officers.

Despite significant developments in ESG integration over the last decade, private equity companies have not standardized their way they manage ESG issues in their investments. Standardization is defined by Malk (2015) as "*applying processes consistently within every stage of the investment cycle*"; meaning for example private equity firms conducting consistent ESG due diligences, and using the same process of measuring and monitoring ESG related issues for each portfolio investment. In their earlier forecasts, Malk (2013) projected a growing standardization of ESG management processes, based on the growing use of uniform due diligence checklists that were not going too deep into specific management processes. In their 2015 report however, Malk found evidence suggesting that ESG management processes are increasingly applied by GPs with a company-by-company approach, dependent on the different material ESG issues identified within each investment. (See next chapter for an explanation of "materiality".) Exemptions from these findings are large private equity firms having already integrated ESG to a great extent, where consistent approaches may be more effective due to the increased public scrutiny (necessitating rigorous follow-up on their ESG commitments), and a greater capacity for ESG management. Also, they may have many portfolio investments that are similar on material ESG dimensions (Malk, 2015). Supporting the trend toward ESG integration being dependent on different investment characteristics, Malk also finds that investors are increasingly leaving it up to the private equity firms to find the method best suited for managing ESG issues. Investors focus on GPs ESG performance is growing, but they focus more on GPs *capacity* for ESG management, rather than requiring certain management methods. "*LPs want to know that GPs are managing ESG effectively, not that they can check a series of boxes*" (Malk, 2015).

Engagement on ESG issues also varies among investors. A 2014 global survey of investors in alternatives by Deutsche Asset & Wealth Management (Deutsche Bank AG), looked at the importance different asset owners put on ESG. They found that high net worth individuals/family offices, banks, pension funds, endowments/foundations and insurance companies place highest overall importance on ESG. However, brokers/dealers took the lead among those who reported that ESG play a major role, arguably because they were among the earlier adopters of ESG strategies. All asset owners report growing in ESG concerns (responses averaging 20%), but high net worth individuals/family offices stands out as almost 60% among them says ESG is gaining in importance. (Deutsche Asset & Wealth Management, 2014).

2.2.5. QUANTIFYING THE IMPACT OF ESG: ADOPTING THE MATERIALITY APPROACH

According to INSEAD (2014), a key challenge for private equity companies today is measuring how ESG initiatives impact portfolio company value. Being able to measure how different ESG activities translate into cash flows, can aid GPs and portfolio company management in concentrating their efforts on relevant non-financial KPIs, and avoid having to spend excessive administrative resources. As outlined by PwC in their 2015 report "Bridging the gap", private equity firms that are able to identify ESG issues having high *material* impact on company value, and have in place processes to properly measure and monitor those impacts, can draw a picture of the value stemming from ESG activities as investments are realized (PwC, 2015). Malk (2015) account for the importance of material assessments, when they argue that in today's investment landscape, where private equity companies have to focus on value creation to a much larger degree (and cannot any longer trust the beta value to drive up price premiums), *"a missing or inaccurate assessment of any material area can diminish, if not tank, an investment*".

The concept of materiality related to ESG derives from the use of the concept in financial reporting, auditing and accounting. Knowledge that has the possibility to influence the decisions of investors are regarded as "material". Similarly, ESG issues that can possibly impact the financial performance of investments are considered "material". In the Global Reporting Initiative guidelines (GRI), the concept is defined in the context of sustainability reporting as aspects that "*Reflect the organization's significant economic, environmental and social impacts; or substantively influence the assessments and decisions of stakeholders.*" (GRI, 2013).

Malk (2015) found that most private equity firms today recognize the material impact ESG risks and opportunities have on company valuations, the same way they assess the materiality of other traditional concerns in investments, such as market trends, competition and operational efficiency. A recent study by ERM (2016) found that 70% of investors have seen ESG issues as having material impact on their portfolio companies (GPs and LPs with investments in PE). Of this total, 60% claimed the material impact stemmed from *protecting value* (in the form of proactive risk mitigation, reduced liabilities and protection of license to operate), and 40% assigned the material impact to the *enhancement of value* (through margin enhancement, brand and reputation, growth and higher exit multiples). ERM further note that *value protection* aspects (for example through reducing absenteeism or control contamination) is easier to assess in a material way than value enhancement aspects (for example company attractiveness to consumers and buyers at exit).

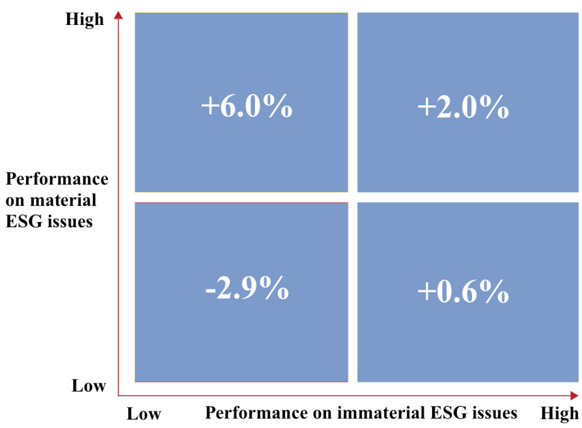


Figure 2: Performance on material & immaterial ESG issues.

A recent and noteworthy study published by Harvard Business Review made an empirical investigation into firm performance on material and immaterial ESG issues, and acknowledges the importance of assessing the materiality to ESG issues and use this as a basis for investment operations. The study addressed ESG concerns that are relevant for value creation (measured by stock prices) in particular public investments, and is the first to point out that firms performing well on *material ESG issues* significantly outperform firms performing well on *immaterial ESG issues*. Further, firms performing well on material ESG issues only, outperform firms performing well on both material and immaterial ESG issues (Khan, Serafeim & Yoon, 2015). The results of the study are visualized in figure 3.

While being able to quantify the impact ESG initiatives have on company value is desired from GPs, with 74% of the respondents in the PwC survey reporting that quantification would be very useful, only 19% of respondents indicate that they currently attempt to quantify the value. This finding is similar to findings in the 2016 UNPRI Report on progress. While 26% are able to measure how ESG performance in investments *change,* only 14% of signatory submissions to the UN PRI Reporting Framework in 2014/15 said that they were measuring the *impact* of ESG on financial performance (UNPRI, 2016b). When it comes to LPs on the other hand, PwC finds that almost all examine GPs ESG strategies before funding decisions, and while they are mostly qualitative, as many as 32% "*assign a quantified ESG weighting to the allocation decision"* (PwC, 2015).

RESEARCH QUESTIONS

When examining ESG integration in the Nordic countries, I first want to clarify what the private equity firms understand by the ESG-concept. Which issues do they see as important to consider in investments? Further, what is the relative importance they give to the three concepts? And which of the issues do the different asset classes prioritize? The understanding of ESG and the weight the firms assign the different issues may in turn impact the extent on ESG integration and the different activities engaged in. To set the stage for my further research I therefore ask:

RQ1: Which ESG factors, if any, do Nordic private equity see as important in investments?

Having established which ESG issues GPs consider as important in investments, I will turn my focus toward the different practices we find in Nordic private equity. Are Nordic GPs following the trend of active management and value creation? Which frameworks do they utilize in their operations? Are they measuring non-financial KPIs, and if so, do they do so consistently? Aiming to map the extent of ESG integration, I ask:

RQ2: To what extent and in which ways are ESG activities integrated into the strategies, procedures and measurements of Nordic PE companies?

The three final research question are developed throughout the following section.

2.3. STRATEGIC DRIVERS AND FUTURE TRAJECTORIES

2.3.1. THE BUSINESS CASE OF ESG IN PE

Various corporate governance characteristics substantiates that the private equity industry is in a favourable position for maximizing the impact of ESG factors in its business operations. Private equity investments have often gone through an extensive Due Diligence process, giving GPs possibility to uncover potential risks and opportunities. Importantly, investments often have long investment horizons (usually being owned for a minimum of four-five years), which gives the investors the possibility to thoroughly implement ESG related changes (Crifo & Forget, 2012). Private equity investors are active shareholders, often acquiring majority or large minority stakes in companies (Novethic, 2009), which gives them advantages over Public investors, whose investor engagement is often considered as "shareholder activism", where they use their voting rights to impact portfolio company management. Moreover, private equity companies bought by a single private equity fund are usually concentrated and few, enabling GPs to obtain deep knowledge of the sector they are investing in, and the possibility to direct considerable time and energy into implementing changes (Novethic, 2009).

A considerable number of research studies have examined the links between ESG and financial performance in public investments. Notable contributions include a meta-analysis by Margolis, Elfenbein & Walsh (2007), presenting slightly positive relations between ESG and profitability. Further, an important and recent contribution by Eccles, Ioannou and Serafeim (2014) conclude that organizations integrating ESG on a voluntary basis ("High Sustainability companies") outperform their peers not integrating such considerations ("Low Sustainability companies") in public markets over an 18-year horizon. The research design allows conclusions to be drawn about causality between ESG and profitability. Important to note however, is that the evidence produced over the last decades on the relationship between ESG and financial performance have been conflicting (Horváthová, 2010). The beforementioned Harvard Business School research addressed this ambiguity, and argued that this is partly because research has overlooked the difference between what counts as "material" and "immaterial" ESG issues. The study contributes to the debate on whether ESG performance impact financial results by advocating that this is the case when companies perform well on *material* ESG issues (Khan, Serafeim & Yoon, 2015). A more detailed description of the findings is found in chapter 2.2.5. When it comes to the link between ESG and fund performance, results have also been mixed. Excluding certain investments from a portfolio might enhance risks because of the limited market exposure, but at the same time, firm selection based on ESG considerations might ensure that the portfolio generate better results in the long term. A comparison between private equity and funds when it comes to the extent of ESG integration is found in the July 2016 Bloomberg Brief, stating that ESG makes faster inroads with private equity than with hedge funds (Morton and Chandler, 2016). The article cites findings from Swiss asset manager Unigestion, on the basis of comparisons between private equity and hedge fund managers. Unigestion uncovered that while 53% of hedge fund managers showed interest in ESG, almost 80% of private equity managers have or are developing ESG programs, and 42% is considered “leaders” or being “advanced” (Unigestion, 2016). Mind, the notations were created by Unigestion on the basis of survey responses. How to quantifying whether a PE firm is a “leader” when it comes to ESG integration is arguably still an open question.

Considering the differences between the investment cycles in public and private equity, it is clear that the financial impact of ESG integration in private equity companies must be analysed differently than the financial impact of public investments. However, most literature that have appeared over the last decades has focused on superior financial performance from investments in listed firms, and there is little research exploring the relationship between value creation through ESG in the private equity industry. According to Scholtens (2006), most literature has given attention to investors in public equity when examining the influences on sustainable corporate behaviour. However, Scholtens note that this focus *“neglects the potential impact of the credit channel and private equity on a firm’s non-financial policies and performance.”* The first empirical work directly linking SRI and private equity, published by Cumming and Johan in 2007, found that investments in socially responsible private equity by institutional investors were likely to increase. A more recent study looks at private equity firms’ adherence to UNPRI between 2006 and 2011 and their associated returns in the US market. The study present empirical results confirming ESG screens in the investment decision ensures higher returns, measured by realized cash multiples for all their investments (Teti, Dell’Acqua and Zocchi, 2012).

2.3.2. DRIVERS OF ESG & SRI IN PE

Reports published on SRI and ESG integration in private equity companies list a variety of drivers fuelling the development. In their 2012 article, researchers Crifo & Forget finds that SRI in private equity is strategically driven, as the management of ESG issues in investment might “*enhance value creation, enlarge risk management and enable private equity firms to differentiate to raise funds”*. In their 2013 report *Putting a price on value*, PwC reported drivers (in decreasing importance) to be *Risk management, Investor pressure, Opportunity, Corporate values, Regulation* and *Senior partner pressure.* (PwC, 2013).

Internal ESG drivers cited in reports and articles notably include risk management; the identification and mitigation of operational risks. The 2015 Malk report finds that risk mitigation is the number one driver of ESG management, more important than elements such as opportunities for growth or cost savings. Common risks cited in the report include unethical and unsafe labour conditions, bribery of foreign officials, environmental liabilities, product hazards, data breaches and regulatory exposure. Following the financial crisis, risk management have also been at the core of the new regulatory reforms (Ioannou, Cornelli & Zhang, 2015). CDC’s Toolkit for Fund Managers stresses the importance of effective risk management, stating that *"opportunities to drive value through enhanced ESG performance (..) should be built on effective ESG risk management"* (The Business Case, n.d.). In recent years however, the private equity industry has been more attentive to the possible opportunities that comes with ESG management (UNPRI, 2014). London Business School lists a variety of value creation opportunities from high ESG performance in their 2015 article, including obtaining better resources and more talented people, achieving better marketing and experiencing increased demand. Cost savings is also highlighted in this context, with companies viewing resource efficiency (concerning water and waste for example) as "*another tool in the toolbox of active management."* (Malk, 2015). The CDC's Toolkit for Fund Managers provides an informative overview of how good ESG management can result in increasing valuation multiples through improving margins and revenue growth. Factors include improved customer loyalty, efficient use of resources and employee retention and productivity. ERM (2016) concludes that as investors are seeing evidence on ESG outperformance, it can *"drive ESG from a 'compliance stick' to a 'carrot' approach in terms of enhanced fundraising.* Malk (2015) note that over the coming years, both firms and portfolio companies will "*see the benefits of incorporating ESG as a differentiator"*.

Looking on pressures driving ESG integration outside of the private equity firms, pressure from investors and fund manager selection is often highlighted. The 2015 London Business School survey concludes that it is the investors, rather than regulatory or governmental pressure that is in the front seat driving ESG integration (Ioannou, Cornelli & Zhang, 2015). Convincing evidence on investor pressure being urgent is provided by PwC (2015), showing that 71% of LPs would decline to participate in fundraising on ESG grounds alone. Similarly, Mercer and LGT Capital Partners surveyed investors with allocations in private equity and found that almost 90% of investors see ESG as a factor in fund manager selection (Mercer & LG TCP, 2015). Moreover, EY (2016) found that investors see private equity firms' ability to handle reporting requirements as the most important factor in fund manager selection. Converting the beliefs into numbers, the late UNPRI Report on Progress show that 78% of LP signatories consider ESG factors to some extent in fund manager selection, appointment and monitoring (UNPRI, 2016b).

After the financial crisis, global financial markets have experienced strong regulatory pressures to ensure financial stability. Requirements concerning risk management and procedures for disclosure has become increasingly important for the private equity industry. Well known regulatory initiatives include the requirement to file "Form PF" under the Dodd-Frank Act, that were passed in the United States in 2010, and reporting requirements under the Alternative Investment Fund Managers Directive (AIFMD) adopted by the European Council in 2011. In their 2016 Global private equity Fund and Investor Survey, EY present a private equity landscape where firms have changed from being performance-driven, into "*organizations poised to rationalize costs while overcoming the burdens of regulatory, investor and* *management reporting"* (EY, 2016). Private equity companies are under increased scrutiny regarding their operations, and other stakeholders such as journalists, NGOs and the general public are requiring GPs to manage ESG effectively and behave responsibly when ESG related incidents happen. Communication platforms such as the social media have given public agents effective tools to hold investors publicly accountable, and investors are increasingly facing the risk of reputational and financial damage if they do not take their license to operate seriously.

Investors' Fiduciary Duties have also been at the core of the ESG integration discussion, as the valuation of a portfolio is subject to the *Fiduciary Duties* of the GP. While the concept of fiduciary duties is defined differently in different countries, the definitions share the same purpose, namely to ensure that managers do not serve their own interests, but act responsibly and in the clients' interests when managing other people's money (UNPRI, 2015). The UNPRI report, "Fiduciary Duty in the 21st Century" established that there are positive duties that falls on GPs to take ESG issues into account in their investments, and with that fuels the pressure to include non-financial considerations in investments.

Initiatives driving ESG integration have also been put forward by industry agents themselves. The Principles for Responsible Investment and the ESG Disclosure Framework for Private Equity are developed by and for investors to promote better ESG practices by the industry. Moreover, Malk presents an important point in their 2015 report: Private equity firms and their portfolio companies are becoming affected by large enterprise customers requiring responsible practices by their supplier companies. These requirements increasingly go beyond standard compliance, and the large companies such as Unilever and Apple are willing to cut ties with companies making headlines on ESG matters (Malk, 2015).

2.3.3. OBSTACLES TO ESG & SRI IN PE

While there are many factors driving the ESG integration momentum, important obstacles are simultaneously hampering the development. To set the stage, the neoclassical view voiced by Milton Friedman (1970) have significantly impacted opinions concerning on non-financial measures for decades. This view advocates that such measures are not part of shareholder responsibilities, and that the costs associated with these activities would result in competitive disadvantage.

ESG management has been viewed as negative or contradictory to private equity operations in many ways. Researchers Teti, Dell'Acqua and Zocchi (2012) present the trade-off concerning disclosure for private equity companies. GPs value discretion and privacy around their investments to avoid spreading information that could ensure superior performance of their investments. At the same time, they feel the pressure to show a willingness to disclose as much as possible to please stakeholders, as measures for ESG compliance are increasingly put forward by industry bodies such as the UN PRI. The 2015 Report on Progress illustrates this, where transparency obtain low scores among GPS investing directly in private companies. A mere 21% disclose ESG information on their investments publicly, and 22% do not even disclose ESG information constituting potential sources of value creation to beneficiaries (UNPRI, 2016b).

Other arguments in disfavour of ESG integration include lack of knowledge and resources. Often, private equity teams are small, and hiring staff dedicated to ESG is not affordable (Gilbert, 2014). Further, collecting good data on ESG developments is critical for GPs, but such collection is both difficult and costly (Ioannou, Cornelli & Zhang, 2015). Structurally, information on Private companies is more difficult to gather than on public companies, and private equity usually targeting smaller companies makes data collection even more difficult (PwC, 2015). As the UN PRIs Guide for General Partners (2014) argue, no universal standard for ESG integration exist and the industry is continuously evolving. GPs are reluctant to integrate ESG practices, due to a "*lack of information on how to begin".* Additionally, it does not help that General Partners are viewing reporting initiatives as "idealistic", and requests posing "administrative hassle" that is mostly concerned with GPs "ticking off in the right boxes" (PwC, 2015).

LPs on the other hand also pose as an obstacle, as they report that they do not know what kind of information that would be relevant for GPs to report on, and hesitate to impose costs on private equity companies with extensive reporting demands. Even if GPs were to disclose, LPs usually do not have the resources to follow up on ESG data from GPs, for example where LPs invest in funds- of-funds and the data volume is large (PwC, 2015).

Ambiguously, as ESG considerations have not been explicitly included in definitions of Fiduciary duties, many investors have claimed that managing money with the interests of other people, does not include integration of non-financial investment criteria. Referrals are often made to the 1985 *Cowan vs. Scargill* case in the UK, ruling out consideration of non-financial issues as part of managers' fiduciary duties (PwC, 2015). Reasons for this reluctance can be attributed to the legal definition of fiduciary duty ("duty to act in another party's interest"), being open to many interpretations. (However, the beforementioned 2015 UNPRI report on fiduciary duties, aims to put an end to investors using the concept as an argument against ESG considerations in investments)

2.3.4. DYNAMICS AND FUTURE TRENDS

The late Global Private Equity Fund and Investor Survey by EY (2016) provides a sound introduction to discussing the dynamics and trends emerging within the private equity universe. The survey portray a market impacted by relentless regulation and investors demanding more data to be reported, quickly. Human resources is required to master new skill sets and talents, such as rapidly adapting to new roles and responsibilities and embracing digital solutions to collect and analyse data. As noted, investor pressure is expected to increase (Malk, 2015), but as the 2016 UNPRI Report on Progress reports, there is a faster proportional growth of private equity firms embracing responsible investments than limited partners (6% vs. 0.9% year-on-year).

As discussed in chapter 2.1.2. *Development of Private Equity*, firms cannot rely on market changes to ensure successful returns the way they used to. To stay on top today, trends among firms include becoming more active and changing operational habits in order to ensure that their investments bear fruit (Malk, 2015).

GPs being active owners is key to understand the future dynamics research is pointing toward. ERM (2016) addressed this trend by acknowledging that firms being most successful in their ESG activities are firms that are able to identify the value creating opportunities stemming from identified material ESG issues across the portfolio. ERM found that only 5% of their surveyed investors believed they had realized the potential value creation opportunities in their portfolio. Malk (2015) support this development and argue that while ESG management is still aimed at responding to investors' demands, an increasing number of private equity firms acknowledge the value protection and enhancement potential that lies in ESG management to the extent that they pursue these objectives *beyond* LPs expectations. When listing "*trends we see on the horizon*", Malk recognizes the opportunity-dimension as one out of three important future trends alongside fund manager selection and adoption of the materiality approach. They consider that ESG management will be increasingly viewed as a value creation opportunity by GPs, both in investments and at the firm level, and especially in terms of innovation and differentiation. INSEAD (2014) and ERM (2016) present various activities enabling effective ESG management in private equity companies. Both reports mention the importance of senior management buy-in/committed leadership and the integration of ESG responsibilities between deal teams and portfolio company management. Training and development of ESG expertize is noted, as well as drawing on the help of consultants and a network of NGOs and industry organizations. Developing flexible ESG frameworks sensitive to both industry trends and portfolio company specifics and the encouragement of best practice sharing between portfolio companies is highlighted. In a similar fashion, McKinsey suggests bringing ESG issues onto investment committee's discussion tables, and the development of industry-wide ESG certifications to signal investment professionals' performance in ESG management (McKinsey, 2016). Diversifying advisory teams to increase the industry expertize provided to portfolio company management is drawn up as especially important in achieving the "operational excellence" needed in an industry characterized by high valuations and tough competition (Johansson, Pettersson & Wireklint, 2016).

The increased focus on active engagement reflects operational changes happening within private equity firms. The move from compliance-focused ESG efforts to viewing it as a source of strategic advantage, signals that private equity companies are making significant changes to their business models (Weide, 2016). In 2013, Malk were early to identify that major private equity companies had begun to *"address ESG concerns...as part of, rather than parallel to, the standard investment process"* (Malk, 2013). As ERM (2016) stresses, for companies to obtain significant value from their ESG initiatives, their engagement need to be deeper than merely embedding ESG processes at firm level and have portfolio companies report on ESG issues. According to UNPRI (2014), effective ESG integration results from combining integration in *investments* with integration into organization *culture, structure and governance*. Without thorough adoption of ESG into the core of the companies, value-add from ESG activities will be hard earned. (As the famous business management "visionary" Peter Drucker stated; "Culture eats strategy for breakfast".) And while some private equity companies have managed to adopt the concept into its core operations and culture, this kind of change takes time, and further developments within company culture and operations is expected. Forbes contributor Kevin Mahn talks about this general trend in investments as the development from "old SRI", namely excluding or including investments for ethical, moral, social or religious reasons, to "new SRI", characterized by investment managers considering ESG factors in a proactive approach towards company operations (Mahn, 2016).

The UNPRI is acknowledging the important role the private equity industry will have in our future societies, and is stepping up its game to make sure investment managers actively follow up on their obligations. As of 2016, its board is considering to develop measures to remove members that have become signatories *simply for show.* (Pearce, 2016). This sends a clear signal to the financial industry that firms have to practice what they preach going forward. Pulling from the other direction is private companies signalling that they want to be run by investors understanding them and their business (Johansson, Pettersson & Wireklint, 2016). Managing partner of Swedish EQT, Thomas von Koch's thoughts on the future of private equity highlights this when he claims that future success of private equity firms will depend on GPs doing business in a way that makes them the "partner of choice" to managers in prospective investments and to investors. He emphasized that in the future, success is not about becoming the biggest firm, but the most reputable (Koch, 2016).

RESEARCH QUESTIONS

Having been through motivations that are commonly listed as drivers for ESG integration, as well as obstacles hindering the integration, I want to look into the strategic drivers and obstacles that are most prevalent in the Nordic private equity industry. I therefore ask:

RQ3: What is the strategic rationales on the part of Nordic PE companies for engaging or not engaging in ESG?

Further, ESG is making its way into investment decisions, and much research assert that ESG is becoming part of company DNA, indicating changes to company operations and value creation strategies. I pose the question:

RQ4: How is ESG integration reflected in Nordic PE company operations and approaches to value creation?

Finally, as macro economic pressures and motivations for pursuing ESG are changing, I want to look into what ESG management will look like in the future. How will General Partners adopt to the changed circumstances, and what will guide and motivate private equity firms in the future? My final query is:

RQ5: What will characterize the future role of the Nordic PE industry with respect to achieving social and environmental objectives?

3. METHODOLOGY

In this chapter, I will give an account for the connection between the purpose of my research and the choice to apply a multiple method research strategy; combining descriptive and exploratory research. Further, the sampling procedures and data collection techniques are described for both the online survey and the semi-structured interviews, before I finally assess the quality of the research method and present ethical considerations.

3.1. PURPOSE AND CHOICE OF METHODOLOGY

3.1.1. SEQUENTIAL EXPLANATORY RESEARCH DESIGN

The purpose of my thesis is to assess the extent and developments of ESG integration in the Nordic private equity industry. The scope of private equity firms I'm targeting is wide, consisting of a range of different types firms applying different ESG strategies, and further the industry is characterized by rapid developments. To pursue my research objective, I've decided on a multiple method research strategy, in the form of a sequential explanatory design, with a qualitative following a quantitative method (Creswell and Clark, 2007).

Primarily, I've applied a quantitative approach to assess the characteristics of the industry with regards to ESG. This approach gives me the opportunity to give an overall assessment of the industry in numbers, and makes the portrayal of the data easily approachable to potential readers. Thus, the main nature of the research is descriptive; aiming at giving an accurate profile of events, persons of situations (Saunders et al, 1997). I employed a survey strategy, collecting data through a questionnaire. This provides an easy and economical way of collecting standardized data that is easy to understand and compare (Saunders et al, 1997), which is helpful when aiming to gather characteristics from a wide range of firms.

In the next phase, I engaged in qualitative research, aiming at providing a richer understanding of the specific dynamics that are happening throughout the industry (as reflected in the research questions 2, 3 and 4). The choice of providing my thesis with a qualitative angle is well suited, as the phenomenon I'm examining is new and complex, and the purpose of qualitative research is to understand and gain insight (Ghauri & Grønhaug, 2010). I conducted qualitative semi-structured interviews with assertive GPs that had shown a particular interest in my research object, singled out by responding to and showing interest in the email initiating them to participate in the survey. The nature of the interviews is exploratory, an approach beneficial for gaining specific insights about a topic of interest (Guest, Namey and Mitchell, 2013). This is particularly relevant as the precise nature of what I'm researching is unclear.

This sequential divide recognizes the nature of the mixed method strategy, where one methodology informs and directs the next phase of data collection and analysis (Saunders et al, 1997). Cresswell and Clark (2007) further state that when combining qualitative and quantitative research, researchers may use the different methods unequally. In this thesis, particular weight is put on the quantitative research, reflecting the research's wide approach, both in terms of companies targeted and topics examined. The following interviews plays a supporting role in explaining the particular findings.

While I've applied a sequential approach, my research is conducted cross sectional rather than longitudinal, providing readers with an exhaustive snapshot into the industry. The follow up interviews were initiated soon after survey completion, and thus, the time span between the execution is ignorable. The rationale for pursuing a multiple methods design is based on a realist conception of reality (existing externally to the world in which we live), reflected in the pursuit of a broad and descriptive understanding of the Nordic industry. However, this position is combined with an appreciation for an interpretivist position (humans are unique social actors, and to study them means to understand how they make sense of the world around them), reflected in the choice adding a qualitative depth to the descriptive findings (Saunders et al, 1997).

3.2. THE THESIS' MAIN STEPS

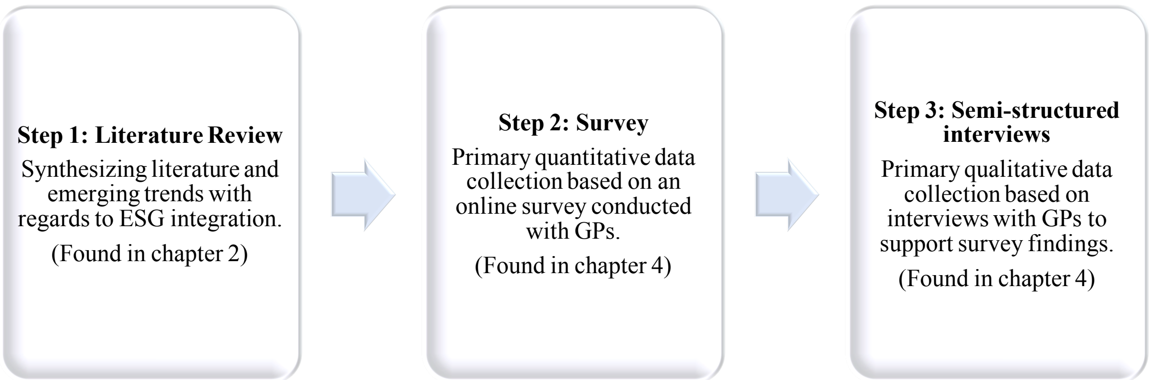


Figure 3: The thesis' main steps

3.2.1. LITERATURE REVIEW

To conduct the literature review, I needed to find literature on the crossing between private equity, socially responsible investments and ESG integration. This intersection is a relatively new field for academic research. As I initiated the search for relevant literature, I found it difficult to locate reliable sources, and what I found was of varying quality and pointed in many directions. As accounted for, the area of research is new, and the amount of academic research is practically non-existent. I have had to rely more on consultancy surveys, reports from industry associations and other non-academic sources.

Therefore, there are limitations to the conclusions (see chapter 6.3. *Research Limitations and Suggestions for Further Research*).

After reading articles I found by chance, I began to form an opinion of what kind of information I would need to present a comprehensive background for my research. I decided to start looking into private equity and characteristics of the Nordic Countries in general. Going forward, I investigated literature debating the nature of the ESG and SRI concepts, and attempted to get an overview of existing ESG practices in the overall private equity industry. While reading various reports and articles, I began noticing commonalities in the findings concerning the motivations for embracing ESG and the developments going forward. These streams of thought formed a unity over time, and now constitutes the final parts of the literature review.

Most of my literature searches were initiated on google, and I often followed leads from lists of suggested further readings in the various reports and articles. This procedure is also known as snowballing; serial reading by following leads in citations and references to new books or articles that provide additional references and so on (Birley & Moreland, 1998). As I began finalizing my literature review I felt that I had gained a comprehensive overview of the state of affairs and main trends.

The full literature review is found in chapter 2. It is logically divided into sections covering background information on private equity and the Nordic countries, definitions of ESG/SRI and the current extent of ESG activities, and finally an overview of strategic reasons for for integrating ESG and changes concerning company operations and future trends.

3.2.2. SURVEY

Survey strategies are associated with making inferences from a certain obtained sample to a larger population (Taylor, Sinha & Goshal, 2006). In order to answer research questions, it is important to identify an appropriate and complete set of cases that the sample is going to represent. The Preqin database on private equity served as my base. Here, I was able to single out active fund managers operating out of the Nordic area.

In the search, I included all investment types, industry focuses, and target regions. According to Preqin there are 283 private equity firms based in the Nordic region as of October 2016. I looked into every firm online, and was able to exclude 48 companies from my total sample. For 14 firms, I did not find any contact information; either no emails or no webpage. Another 14 firms were no longer in operation, were shutting down operations or made no more investments. Finally, I decided that 20 firms were not relevant for my study, being for example providers of advice to institutional investors or had shifted focus to public markets. This left me with a total sample frame of 235 private equity Firms with their headquarters in the Nordic countries, 83 Swedish, 57 Finnish, 42 Danish, 41 Norwegian, 11 Icelandic and one firm from Greenland. Note that I looked at the private equity *firm level*, and not the *fund level*. The firms, and more likely the larger ones may manage multiple funds.

When generalizing from responses obtained to the population it is supposed to represent, it is desirable that the response rate is as large as possible, lowering the chances of making errors when generalizing to the population (Saunders et al, 1997). I obtained a response rate of 25,53% (60 respondents out of 235 firms). Comparing my rate to similar studies (looking at the private equity industry and ESG considerations/socially responsible investments), I consider 25,5% to be a favourable outcome. Cumming and Johan (2007) obtained a 7% response rate (100 respondents out of 1114 Dutch institutional investors) when examining SRI in institutional investments. BVCA (2009) obtained a 20% response rate (84 respondents out of 415 firms in the UK) when addressing BVCA members' views on investing habits and sustainability. Cumming and Zambelli (2010, 2012) obtained a 47% response rate (27 respondents out of 57 PE funds in Italy) when comparing regulations on Limited Buyouts. Finally, Crifo & Forget (2012) obtained a response rate of 24.0% (74 respondents out of 308 firms) when researching French private equity firms and ESG integration. While I find an overrepresentation of Norwegian companies, I argue that my sample is representative of the Nordic industry due to the relative spread of the responses over the other countries. (A discussion concerning self-selection and other biases are found in chapter 5.3. *Research Limitations and Suggestions for Further Research.*)

Based on findings in recent articles/reports, I developed an understanding for what type of questions that would be relevant to ask the Nordic industry to be able to map the extent of ESG integration and point toward trends. I had several informal conversations concerning which questions to ask with GPs familiar to ESG issues, including Reynir Indahl of Swedish Summa Equity and Jon Fredrik Vassengen of Norwegian Argentum. These conversations provided me with important insights, and helped me broaden my understanding of the Nordic PE industry so I would not leave out important elements, and sharpen my questions so that they would pinpoint the specific industry dynamics. The final survey consisted of 35 questions (found in the appendix). They were all closed-ended, providing a final set of responses which the respondents were to choose between. By posing closed questions, I simplified the process of understanding of the responses, which in turn were beneficial in the following data analysis. I was anxious to make sure no questions could be misunderstood, and I placed all the explicitly descriptive routine questions at the end (such as fund manager location, amount of AUM and so on) as not to tire participants and make them quit the survey before completion.

After finalizing the online survey in the web program "Qualtrics", I conducted a test round in October. The aim of the test was to find out whether the sequencing and the form of the questions I had developed made sense in the online format, and also whether the program was functioning properly. The test survey was distributed to GPs from the Norwegian private equity firms HitecVision and Argentum. They provided valuable feedback on the flow and workings of the survey as they went through the survey, page for page. The feedback was given over the phone, via email and in person.

The execution of the survey took place over the course of three weeks in the beginning of November. The first week, I sent an email explaining the purpose of the survey and the link to the online survey to one member from each of the 235 private equity firms in my sample frame, singled out from firm websites. When the week had passed, I had obtained 12 responses. The following week I did another search through homepages, singled out and sent the email with the survey link to one or more team members relevant for the purposes of my study. This approach led to 34 additional responses. I left the survey open for responses one final week, while contacting companies that had implied that they would answer at a later time, or that someone else on the team were to participate. When I closed the survey, the total number of respondents, complete and incomplete were 118. Out of these 118 I first deleted the responses where the survey had been opened but not commenced (41). Then I deleted duplicates (3), where I had gotten more than one response from a certain firm (I included the first response obtained). Finally, I deleted partial responses (14). Left were 60 unique responses (25.53%) from firms from all Nordic countries representing a wide range of private equity stages and sectors.

3.2.3. INTERVIEWS

To provide my thesis with additional depth, I examined the reasons behind the participants' attitudes and opinions uncovered in the survey on the topics of motivations, operational and cultural changes within the firms, and future trends. I conducted five interviews with representatives from private equity firms that showed a particular interest for the research objectives when they received and answered to the survey email. The reason for the participant sample were moreover based on the participants' websites and public image. I targeted companies where sustainability and ESG integration was very much on the agenda. In order to provide diversity, weight was finally put on selecting companies representing a broad geographical scope. The final interviewee sample includes representatives from two Swedish firms, one from Denmark, one from Iceland and one from Norway. The sample size of five corresponds to the minimum number of participants for a meaningful semi structured interview-analysis (Saunders et al, 1997). Saunders mentions that the suitable sample size depends on the purposes of the research, and considering the subordinate status the interview has in my thesis, I further argue that the smaller sample size is suitable.

Company	Country	Interviewee	Position	Duration	Date
Axcel	Denmark	Christian Sinding	Investor Relations Officer	20 minutes	November 29th, 2016
Ratos	Sweden	Jenny Askfelt Ruud	Head of Sustainability	15 minutes	November 30th, 2016
EQT	Sweden	Therése Lennehag	Head of Responsible Investment	20 minutes	December 13th, 2016
Virding	Iceland	Margit Robertet	Managing Director: Private Equity	25 minutes	December 1st, 2016
FSN Capital	Norway	Morten Wælo	Partner & Chief Operating Officer/Investor Relations	25 minutes	December 6th, 2016

Table 2: Overview of interviewees

I chose to conduct semi-structured interviews to gather primary data on the different areas of interest. Semi-structured interviews are characterized by the researcher approaching the interviewee with a list of key questions covering key themes, but allow for additional questions to be asked to explore research questions further (Ghauri & Grønhaug, 2005). This approach lets the interviewees speak more freely than in a structured interview, where the interviewer asks a predetermined and identical set of questions. Semi structured interviews gave me the opportunity to ask follow-up questions where I felt the participants had more important insights to provide. Further, it lays some constraints on the direction of the interview, which ensured that the course of the conversation stayed within the themes included in the research questions. I therefore argue that the semi-structured approach was advantageous to my research.

As mentioned, the interview questions were centred around the three final research questions having to do with the companies' motivations, operations and future beliefs. The specific questions were chosen for multiple reasons. Primarily, they were chosen on the basis of the synthesized literature on dynamics and future trends in the industry. They followed up on alleged trends such as ESG developing into being part of the companies' DNA, and the need to recruit people with different skill sets. Further, they were chosen because the final research questions begs for a more in-depth analysis. Where the survey questions covering company practices related to ESG are more technical, the questions targeting General Partners beliefs when it comes to motivations, operations and future characteristics would benefit from a more nuanced and complex portrayal. I therefore argue that a semi-structured interview is suitable approach. I formulated open questions, using phrases such as "*How would you describe...*", "*How would you say...*" and "*What are your thoughts on…*", encouraging participants to answer in accordance with their interpretation of the question, and to emphasise what they thought were important in relation to the different themes.

Before the interviews took place, I sent each participant an interview guide, so they would get an idea of the different topics I wanted to investigate. The questions were developed with the aim of triggering responses that would provide insights to the research questions. Apart from the questions, the guide also included general information about my research objective, as well as practical information such as the participants' anonymity.

During the interviews, introductions were officially made, and I explained my reasons for choosing each specific participant. Issues concerning anonymity were agreed upon, as well as procedures for data recording, storage and transcription. Before commencing with the questions, Interviewees understood my research objective and seemed comfortable with both the telephone-interview setting and the themes we were to talk about. Shortly after the interviews, I sent the participants transcripts of the interviews together with an encouragement to review them and make sure my interpretation of their comments were correct.

When analysing the interview, the specific answers were coded according the themes contained in research questions 3-5, and analysed based on my own understanding of the different themes. Findings from the interviews, as well as illustrative quotes are found in connection with the specific research questions they reflect in section 4.2. Illustrative quotes are moreover used in the discussion chapter. The interview guide is found in the appendix (chapter 8.1), together with the full answers from the interviews (chapter 8.3). Mind, the interview participants were reluctant concerning firm- attribution of their statements. The statements included in this thesis are therefore anonymous, except from the statement from EQT on page 8 which I was permitted to name.

3.3. ASSESSMENT OF QUALITY

To make sure the results of the study are trustworthy, the reliability and validity of the procedures used in the research is examined. Further discussions on possible limitations of my study is found in chapter 5.3. *Research Limitations and Suggestions for Further Research.*

3.3.1. RELIABILITY

Reliability concerns whether the research design (the techniques to collect and analyse data), is carefully chosen and described, in order to generate the same findings if carried out by another researcher or on another occasion (Saunders et al, 1997). The study is providing a descriptive snapshot of ESG integration in Nordic private equity industry at the time of writing. ESG integration however, is an emerging topic, where substantial and rapid changes characterize the development. Due to these dynamics, reliability is threatened as it is likely that conducting the research at a later time would produce different results. Further, I've conducted the study alone, which may have had a negative impact on the objectivity in the data analysis.

Reliability related to conducting a survey concerns the consistency of the questions posed, that they cannot be interpreted in different ways by different participants. As I spent two months learning about the industry before I wrote the questions, and had GPs helping me assess my questions, I argue that I limited the possibility of threats to reliability in the survey. Reliability issues associated with the semi-structured interviews commonly include the lack of standardization of the interview settings, making the possibility to recreate the situations and obtain the same answers difficult. The fact they the interviews were conducted on different times of the day, might have impacted answers they gave. Also, my attitude and tone in asking the questions may have impacted the direction of the participants' answers. On their part, they might have response biases due to the intrusive nature of the semi structure-form. This could especially hold true for private equity firms, as they traditionally are perceived as being more secretive about their operational choices. However, I did not sense any particular hesitation in their responses, or reluctance to answer specific questions.

3.3.2. VALIDITY

Validity regarding findings concern that they are really about what they appear to be about (Robson, 2002). A valid questionnaire generates accurate data that correctly measures the concepts it is meant to be measuring (Saunders et al, 1997). In designing a questionnaire, Saunders et al. recommend using an online survey tool such as SurveyMonkey. I have utilized a similar online program, "Qualtrics", that has a layout design with NHH's logo, and thus ensures an additional layer of trust in the survey. In my survey, the most obvious concepts that could be misinterpreted include "ESG" and "SRI". To avoid any confusion, I explained the meanings of these abbreviations to the participants prior to taking the survey.

External validity, also named "generalizability", concerns the degree findings are applicable to other situations (Robson, 2002). In my case, I would for example prove external validity if similar results could be obtained on ESG integration in other geographical areas. While replicating the study in another context would be difficult, I have noted that my results are comparable to results obtained by recognized research done on ESG integration in private equity to a large extent. Examples include Patricia Crifo & Vanina Forget's (2013) research on ESG integration in the French private equity industry, and the 2015 London Business School research mapping ESG integration in investment processes based on a global sample.

Internal validity when doing research based on a survey-strategy, deals with the relation between the questions asked and the outcome, that the questions asked adequately cover what is implied by the constructs (Saunders et al, 1997). Threats to internal validity that may have impacted my study include changes or unforeseen events that may have changed the participants' views and behaviours, resulting in the apparent relation uncovered in reality is due to some other reason. However, I believe the short timespan of data collection (slightly over two weeks), ensured that no events (internally or externally in the companies) could have altered their responses significantly. Further, by pilot testing the survey with industry professionals and learning whether the survey "made sense", I ensured that the questionnaire obtained degrees of face validity (Saunders et al, 1997).

Validity in semi-structured interviews concern the extent researchers are able to infer the correct meanings from the words the interviewee participants are using and credibly presenting this to the readers (Kuzmanić, 2009). As the interviews were conducted late in the writing process, I argue that I have limited the risk of such validity on the grounds that I have had months gaining knowledge and insights into the workings of the Nordic private equity industry, and have gained a fair understanding of important concepts as well as industry jargon. Further I was careful to clarify the questions asked, often restating the questions using different words, or leading the interviewees back to the questions' intended meaning should they initiate answers based on misunderstandings.

It is important to note that responding to my survey was completely voluntary. Those who responded to my survey may have been companies that already have a sound ESG agenda in place, and because of that are interested in being part of the research. I therefore advise the readers to have this in mind when studying the results. (See further comments on survey limitations in chapter 6.3. *Research Limitations and Suggestions for Further Research*.)

3.5. ETHICAL CONSIDERATIONS

Research ethics is defined as the standards and behaviours that guide conduct in relation to the rights of those who become the subject- or is affected by the research (Saunders et al, 1997).

In writing my thesis, I have been especially careful to consider ethical concerns that may have arisen when gaining access to survey and interview participants. Early in the process I considered whether my survey data collection would violate to the Norwegian Personal Data Act, regulating the collection and procession of personal data (http://www.nsd.uib.no/personvern/en/). As I only needed information from the participants on the country where their Headquarters were located (which was formulated as a question in the survey), I avoided the personal data issue. I made the survey anonymous, and invited the participant to take the survey via an anonymous link.

Based on the overview of private equity Fund Managers based in the Nordic countries, I examined the webpages of each company to find the most suitable person/persons to contact. I could not control who finally completed the surveys, but to limit the possibility of multiple answers from the same company, I included in the survey a question about the respondents' company. I informed the participants that the company name would not be included in the final dataset, and they also had the option to leave it blank.

This measure may also have aided increasing the internal validity of the thesis (respondents giving true responses) by reassuring them that their answers would not result in consequences on their behalf.

Before commencing both the survey and the interviews, I made sure participants were informed about the purpose of my thesis. Further, In the survey invitation, I gave the participants reassurance on the anonymity of their responses, and before commencing the interviews, I asked for and got permission to use the interview answers in my thesis. I made sure that they could vouch for the quotes and extracts I would use throughout my thesis by providing transcripts from the interviews which they could revise to make sure their answers would accurately reflect their true opinion. As mentioned, the interviewees were concerned regarding the attribution of firm name to their statements. Therefore, I made sure that the quotes found in the results- and discussion section as well as in the appendix are completely anonymized.

Moreover, I have considered more general concerns throughout the writing process. The main research objective, both the crossing of ESG and private equity and the focus on the Nordic industry, has sprung out of my own interest in the area of Sustainability in business, and is not influenced by external parties. Communication on the different research areas with my supervisor and knowledgeable individuals have supported the development and direction of my research, but I have made an effort to make continual critical assessments of my own choices and reflections.

4. ANALYSIS AND FINDINGS

In this chapter, I will go chronologically trough the research questions and provide findings from the online survey and semi-structured interviews. Findings form the semi-structured interviews are included in relation to research questions 3, 4 and 5. To begin with, I will present descriptive statistics introducing the readers to the sample of firms responding to the survey. (The sample profile from the interviews is found in chapter 3.2.3: *Interviews*.) Euro is adopted as default currency throughout the results.

4.1. DESCRIPTIVE STATISTICS

Response rates. The total response rate obtained: 60 firms out of 235 firms (25.53%).
Divided into the specific countries:

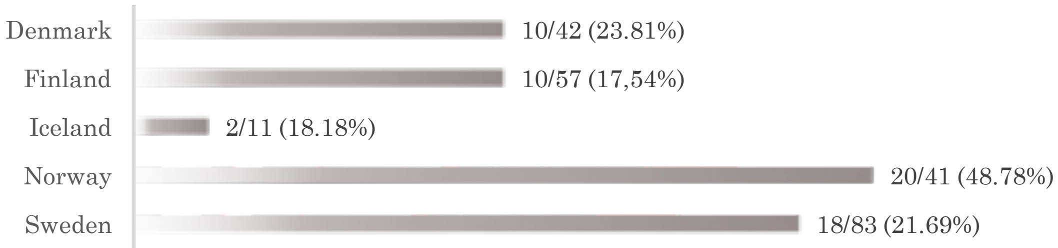


Figure 4: Responses by country

Type of asset class. My obtained response sample consists of firms representing various private equity types. Notably, respondents represented buyout, growth and venture capital firms. (Companies were allowed to choose more than one investment type. Total number of respondents: 77)

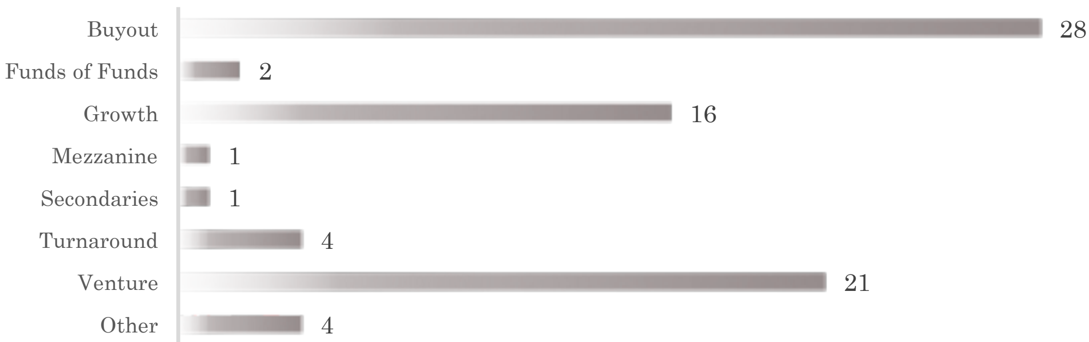


Figure 5: Responses by asset class

Assets under management (AUM). Based on the size of the Nordic industry, I choose the lesser category of AUM to be €500 Mn and below, after looking into the lesser category (below $1 Bn) in London Business School's 2015 survey on the increased presence of ESG in the investment process. My sample shows an overrepresentation of smaller firms.
(Total number of respondents: 59)

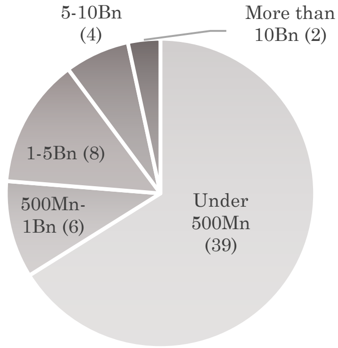


Figure 6: Responses by assets under management

Average size of investment. My sample shows an overrepresentation of firms making smaller investments.
(Total number of respondents: 58)

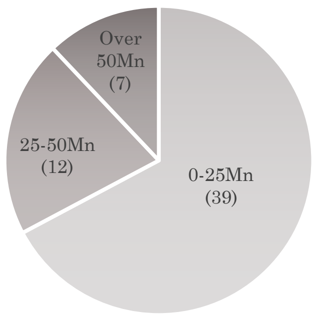


Figure 7: Responses by average size of investments

Sector focus. My questionnaire further enquired about sector/industry preferences. Sectors are borrowed from Argentums Market database's. Companies were allowed to choose more than one industry.
(Total number of responses: 128)

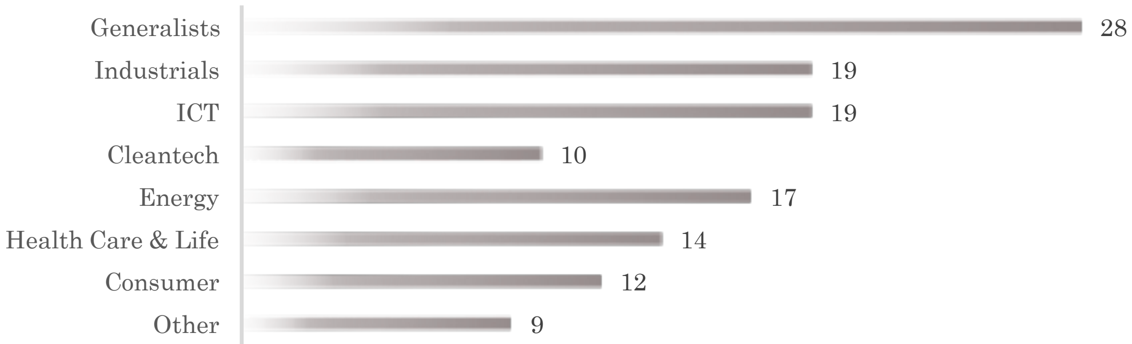


Figure 8: Responses by industry preferences

Headcount. The respondents mainly represented smaller firms, with 62% of the teams consisting of 10 people or less. However, a considerable part of the responses represented teams of 20 or more people (22%). (Total number of respondents: 60)

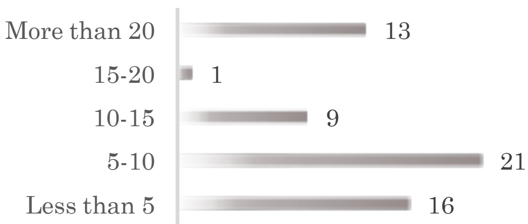


Figure 9: Responses by team headcount

Male/female ratio. No respondents reported an all female team. 1 firm (1.67%) reported mostly female, 8 firms (13.33%) reported 50%50, 39 firms (65.00%) reported mostly male and 12 firms (20.00%) reported an all male team. (Total number of respondents: 60)

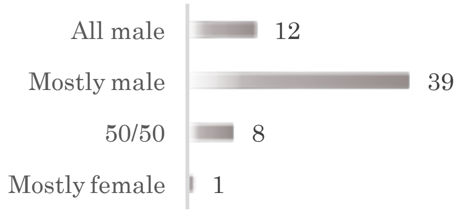


Figure 10: Responses by team gender composition

Overall, I find an overrepresentation of Norwegian firms, likely due to the recognition effect of using labels such as the Norwegian School of Economics (NHH) and The Argentum Centre for Private Equity (which is located at NHH) in the email invitations to participate in the survey. Further, smaller firms are overrepresented, doing smaller deals. There is more of a uniform distribution of firm types and industry preferences. Looking into headcount, teams of all sizes have responded the survey, but smaller teams are overrepresented. Finally, I find that most respondents represent teams comprised of mostly male GPs. Taken together, I conclude that my obtained sample adequately represents the Nordic private equity industry.

RQ1: ESG

Which ESG factors, if any, do Nordic private equity see as important in investments?

Due to the numerous different approaches for ESG integration, frameworks applied and geographic locations, what the concept of "ESG" contains is viewed differently from GP to GP. Before examining the various ESG related strategies and beliefs among GPs in the Nordic countries, I presented the survey participants with lists of potential ESG issues and asked them to indicate which of them they perceive as most important in investments. I applied the list of examples of ESG factors presented in UNPRI's Guide to Limited Partners (2011), which is also found in UNPRI (2014) Guide to General Partners. Companies were encouraged to choose multiple issues, but no more than 5. Top five choices within the different categories (Environment, Social and Governance) are illustrated in figure 11.

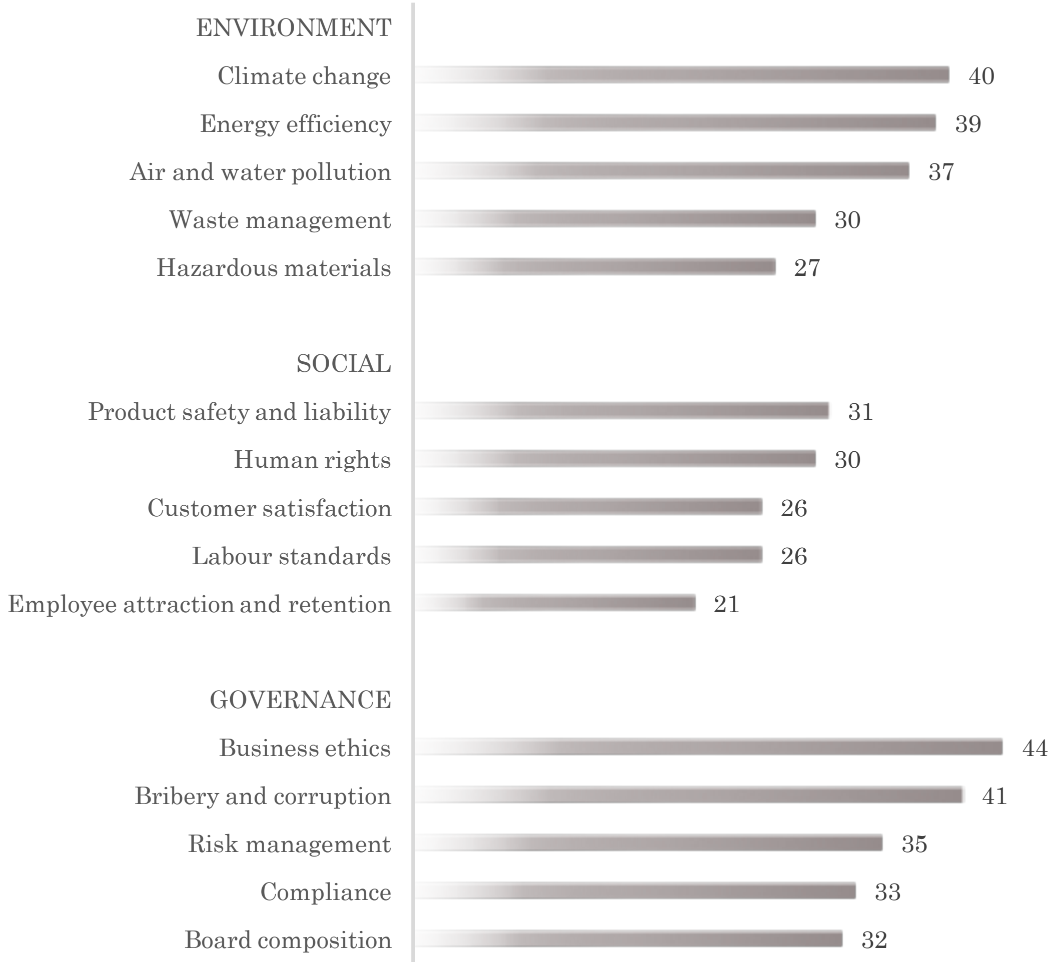


Figure 11: Importance of specific ESG issues in investments

Environmental issues got a total vote count of 215, social 240 and governance 255. The higher scores for the environmental and governance issues seen above indicate stronger coherence among GPs on these issues, and especially so for environmental issues, which received the smallest number of votes.

Nuancing the value GPs put on the specific ESG issues in investments, I followed up by enquiring about the relative importance given to the different issues. I asked GPs to rank the issues according to their regard of the importance, and the results indicate that Governance issues are most frequently regarded as most important, with Environmental issues following. Social issues were most frequently given second priority. Interesting to see is that Environmental issues often appear last in GPs priorities.

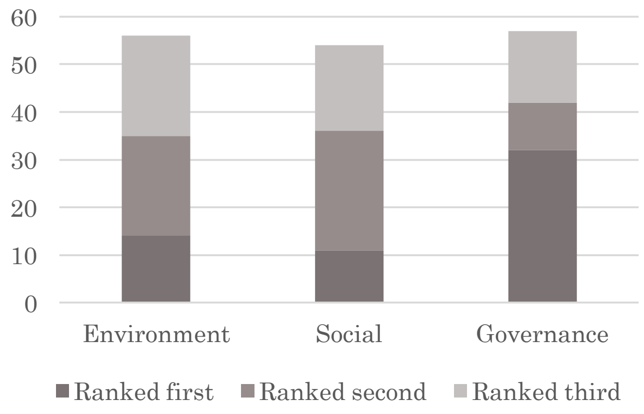


Figure 12: Relative importance of ESG issues in investments

Based on this finding, I looked into what the different asset classes gave top priority. My response rates were dominated by Buyout (28), Venture Capital (21) and Growth Capital (16), accounting for 85% of the responses, and I therefore looked into those asset classes. (Mind, GPs could choose multiple asset classes. By the 60 respondents, 77 responses were reported.) Buyout funds most often give Governance issues top priority, with Social and Environmental issues following. Venture and growth funds most often assign Governance issues top priority as well, but for them Environmental issues are more often than Social issues given top priority. Notice that Governance issues do not take a significant lead in among growth funds.

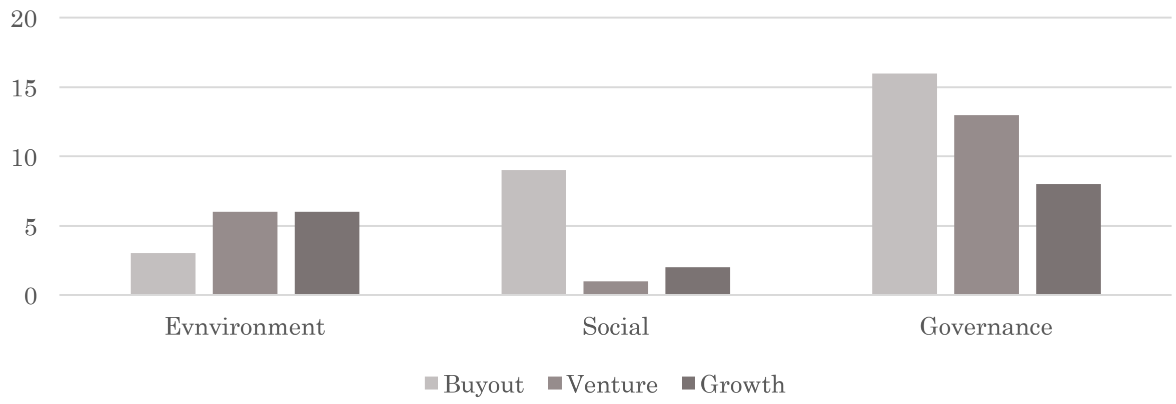


Figure 13: Prioritized ESG issues by asset class

RQ2: EXTENT OF INTEGRATION

To what extent and in which ways are ESG activities integrated into the strategies, procedures and measurements of Nordic PE companies?

Standards and policies

65% of firms surveyed (39 firms) agree that ESG is an important part of their company's agenda. Including companies somewhat agreeing, this number illustrate the views of exactly 90% of Nordic companies. Almost 70% (41 firms) indicate that they have established standards for Socially Responsible Investment, and an additional 13% (8 firms) report that such standards are in development. Only 18% (11 firms) report that they don't have a policy. While policies may not be verbally laid out, firms may still apply different ESG related strategies in the screening process of potential investment. 44 firms (73%) apply negative screening in the investment decision process, e.g. avoiding companies affiliated with alcohol, tobacco, guns or gambling, or apply a worst-in-class strategy, excluding companies that show poor ESG performance. 25 firms (42%) apply positive screening strategies, such as active inclusion of companies with strong ESG follow-up, or apply a best-in-class strategy, aiming at investing in the companies performing best on ESG matters. 18 firms (30%) apply both strategies. Only 9 (15%) of the 60 firms surveyed do not apply any of these strategies (firms were allowed to choose both strategies).

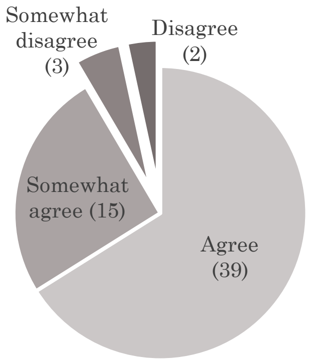


Figure 14: *"ESG is an important part of our company's agenda"*

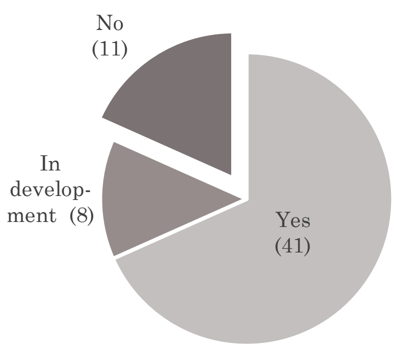


Figure 15: *"Do you have a policy or established standards for Socially Responsible Investments?"*

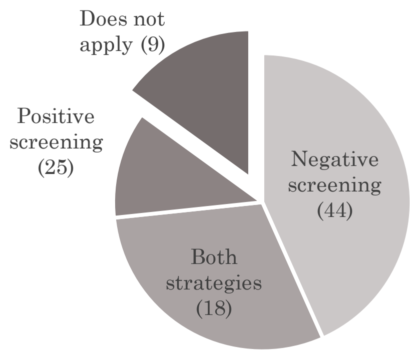


Figure 16: ESG strategies applied

Frameworks and guidelines applied show that Nordic PE firms turn to a variety of sources for aid in the integration and management of ESG.

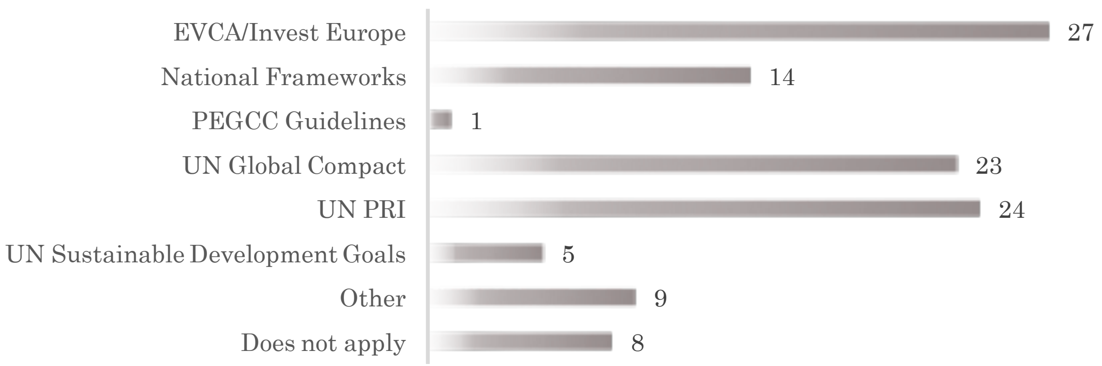


Figure 17: Frameworks and guidelines applied within Nordic private equity

Integration in operations

Evidence on the extent of ESG integration can come from various sources. First, I wanted to look at where the responsibilities for integration is placed; whether Nordic companies have hired staff specifically for ESG purposes, or if the responsibilities lie within the duties of other personnel. I found that 45% of firms assign ESG responsibilities to *Investment Professionals*, and 20% of the firms assign responsibilities to the *Managing Partners*. *ESG professionals* are charged with the responsibilities for 10% of the firms, and for 5%, the responsibilities lie with the *COO/Head of IR*. 15% of companies report that the responsibilities lie elsewhere. See figure 17. Next I looked into the importance GPs put on ESG considerations in the different investment phases. Being asked to assess the importance put on ESG in the different phases on a scale from 1-5, Nordic companies reported that they put most weigh in ESG consideration during Board follow up/Ownership, with a mean of 3.97. Following are ESG considerations in Due Diligence (mean: 3.80), and in Exit (mean: 3.46). Nordic PE companies thus confirm that they are working with ESG during all of the different investment phases.

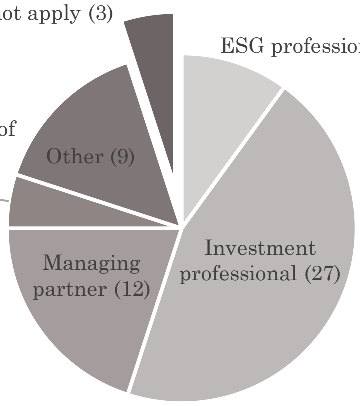


Figure 18: Placement of ESG responsibilities

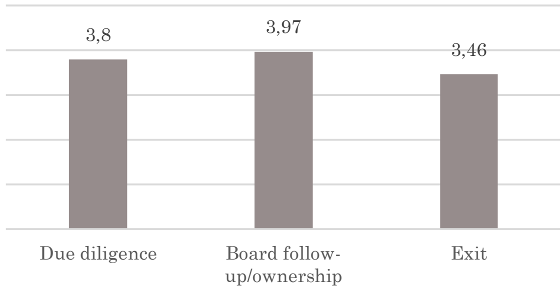
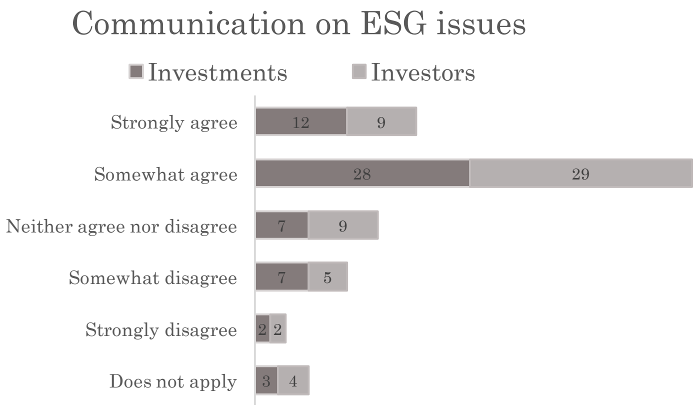


Figure 19: Weight put on ESG in different investment phases (mean)

This further begs the question: How are they making sure investors on one hand is updated on ESG developments, and portfolio company management on the other is included in the promotion of ESG issues? Faced with questions about their communication habits, 68% (40 firms) agree to have frequent communication with investors regarding ESG related issues, and 66% (38 firms) to have frequent communication with portfolio company management (GPs answers including Somewhat agree and Strongly agree to the statement). Finally, while their commitments today show that they do take ESG issues seriously, I enquired about what the firms expect to be their resource allocation to ESG activities (e.g. time, money, human resources) three years from now. No firm believed their allocation would decrease. 45 firms indicated that they expected their allocations to increase, and 14 firms reported that they would have no changes in resource allocations.



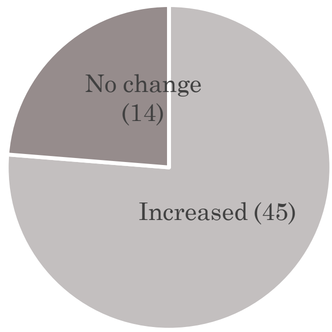
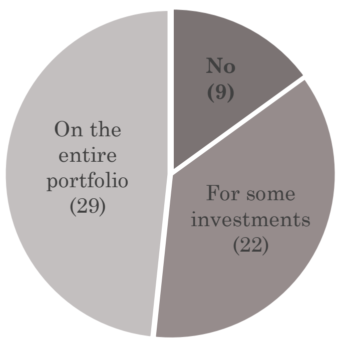


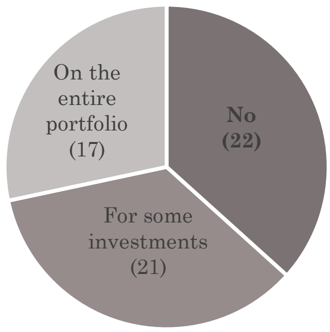
Figure 20: Agreement with the statement: *"We have frequent communication regarding ESG related issues with..."*

Figure 21: Expected resource alloxation to ESG activities

Measurements

Being able to measure non-financial KPIs related to ESG activities in investments is something GPs strive for. 51 (85%) of of the 60 firms consider the materiality of ESG concerns, and out of these, 29 firms (almost 50%) do so for the entire portfolio. I further found that 38 firms (63%) out of 60 are measuring non-financial KPIs today, with 17 firms out of these doing so on their entire portfolio.





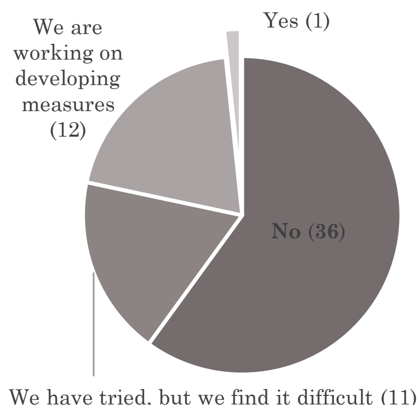


Figure 22: Material assessments of ESG concerns

Figure 23: Measurement of non-financial KPIs

Figure 24: Measurement af ESG activities' impact on financial performance

It is further interesting to look at whether the firms are able to assess the financial contributions of their ESG activities. Among the Nordic firms, only one firm report to successfully measure the impact. 12 firms are developing procedures for doing so, 12 more have tried, but found it to difficult, and 36 firms are not quantifying the impact. While not claiming to assess the explicit financial impact, 32 firms (53%) say that ESG activities have improved their risk situation, and 12 firms (20%) say the same about company valuations. Further, based on the significant finding by Malk (2015) showing that GPs choose when and how to apply ESG management with a company-by-company approach, I wanted to see if Nordic PE companies are mirroring this trend. Of the firms giving a positive response (42), I found that

13 firms (31%) use a consistent/uniform approach for all investments, while 29 firms (69%) develop KPIs on a company-by-company basis. While the industry is moving forward on ESG integration, I wanted to see whether some Nordic PE firms go beyond traditional measurement procedures and assess whether their ESG performance have an impact on the UN Sustainable Development Goals.

Figure 25: Approach to ESG management

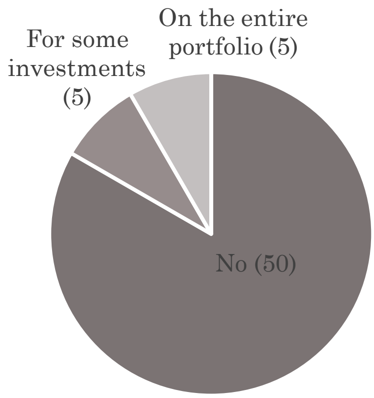


Figure 26: Assessment of impact on the SDGs

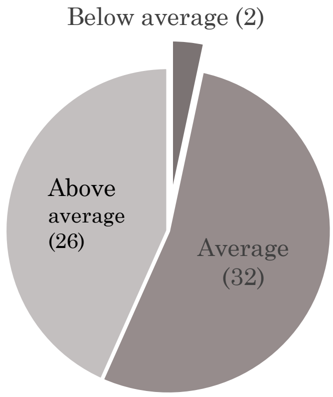


Figure: Beliefs on ESG performance compared to the Nordic average

Partly because the goals are fairly new, I did not expect a large turnout. 10 out of the 60 firms however report that they assess the impact their ESG activities has on the UN SDGs, and five out of them make such assessments on their entire portfolio. Interestingly, when asked about how they believe their company's ESG performance compares to the industry average in the Nordic region, 58 out of the 60 firms think they perform average or above.

RQ3: DRIVERS AND OBSTACLES

What is the strategic rationales on the part of Nordic PE companies for engaging or not engaging in ESG?

What reasoning lie behind Nordic PE's choices to engage in ESG management? By and large all of the firms surveyed agree that they focus on ESG to ensure long term success (see figure 23), but which strategic drivers are motivating their actions, and what do they perceive as the most important obstacles facing their integration?

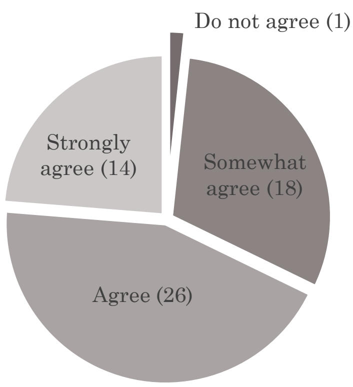


Figure 27: Agreement with the statement: *"We focus on ESG to ensure long term success"*

External ESG drivers

First, I enquired about drivers of ESG integration from *outside* the company. GPs could choose the drivers that applied. The bars represent the rank they gave the different drivers.

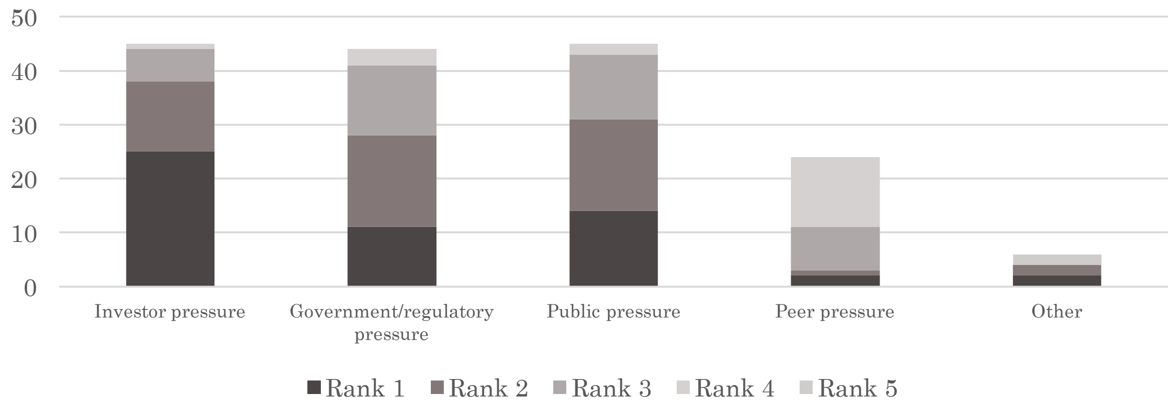


Figure 28: External ESG drivers

From the chart, we see that most GPs view *Investor pressure* as the most potent driver for ESG integration. Following close are *Public pressure* and *Government/Regulatory* pressure. *Peer pressure* were noticeably less regarded as driving their ESG efforts. Illustrating the importance GPs put on Investors, 82% believe the ESG focus among investors to have increased three years from now, and the remaining 18% expected no change. GPs further believe that in three years, Investors will require that GPs have made various commitments regarding ESG. Related to policies and frameworks, 43 firms (71%) expect they will have to have an ESG policy, and 34 firms (57%) expect having to show a commitment to industry standards (UNPRI, Invest Europe etc.).

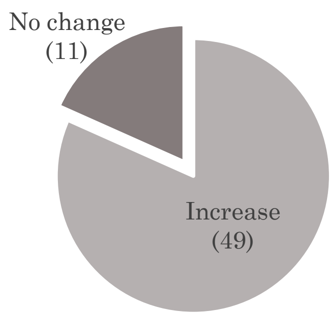


Figure 29: LPs focus on ESG three years from now

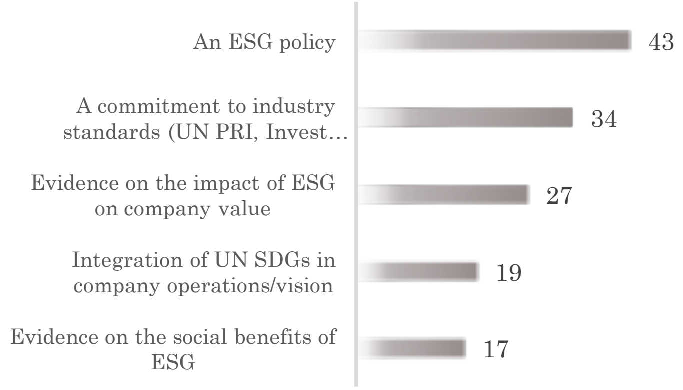


Figure 30: Expected LP requirements related to ESG three years from now

Regarding financial performance, 27 firms (45%) report they expect to have to show evidence on the impact of ESG on company value. With regard to social performance, 19 firms (32%) believe they will have to show that they have integrated the UN Sustainable Development Goals in company operations/vision, and 17 firms (28%) that they will have to show evidence on the societal benefits of ESG.

Internal ESG drivers

Next I analysed drivers of ESG integration from *inside* the company. GPs could choose the drivers that applied, and give each a score from 1-5. The bars represent which rank they gave the different drivers.

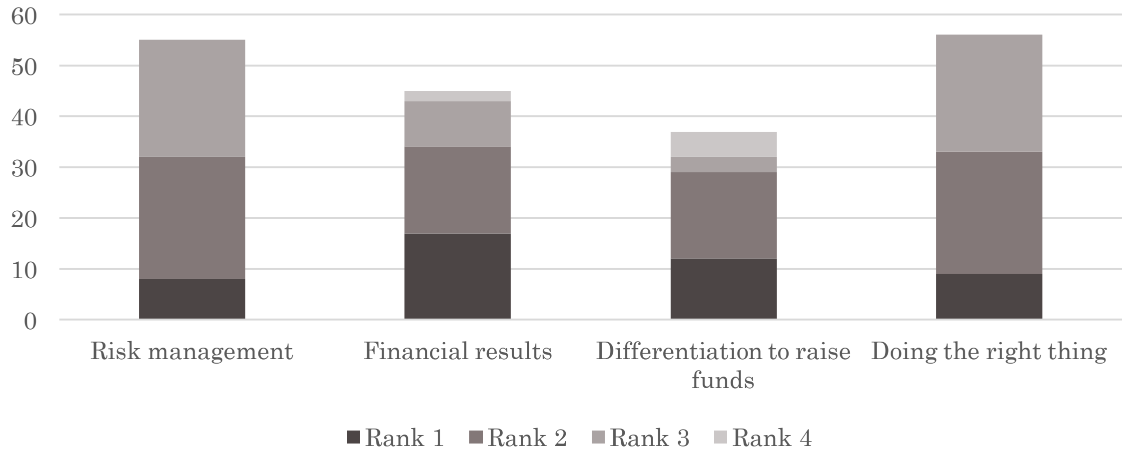


Figure 31: Internal ESG drivers

From the chart, we see that most GPs rank the possibility to obtain *Financial results* as the primary driver, followed by *Differentiation to raise* funds and *Risk management*. Looking at the cumulative scores however, *Risk management* stands out, indicating that for more of the investors, internal motivations include risk management. As the results show, GPs are additionally integrating ESG on the grounds of *Doing the right thing* to a significant extent.

Obstacles to ESG integration

Lastly, contrasting the examination of drivers to ESG integration, I looked at what GPs perceive as the biggest obstacles to their work on ESG integration. GPs could choose the obstacles that applied. The bars represent which rank they gave the different drivers.

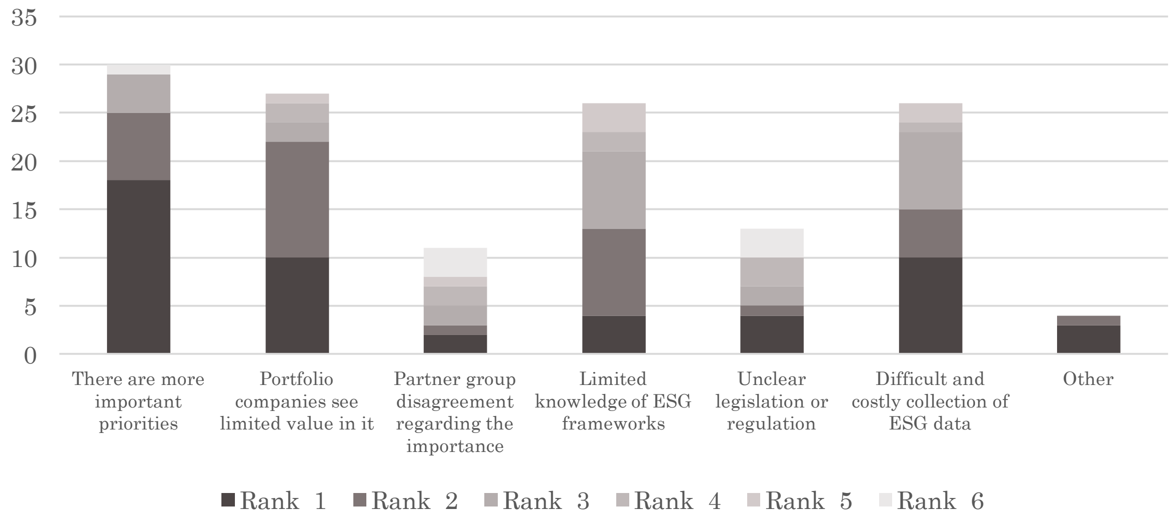


Figure 32: Obstacles to ESG integration

Most GPs indicate that more important priorities constitute the biggest obstacle to ESG integration. Challenges with portfolio companies not seeing value in ESG integration and hurdles associated with the collection of ESG data follow. Limited knowledge of ESG frameworks is also an important obstacle, but less often viewed as the main impediment. Disagreements among partners regarding the importance and vague regulations and legislations score considerably lower.

Findings from the interviews

The main question investigating GPs thoughts on the motivations for ESG integration asked for thoughts on ESG integration being a competitive advantage. However, GPs talking about motivations to ESG while answering other questions as well. Below are themes that commonly appeared in the GPs responses concerning motivations. The full responses related to the themes are found in the appendix, chapter 8.3.

Performance and outperformance is commonly highlighted as motivating companies' ESG efforts. Interviewees talked about ESG management resulting in improved investment decisions, increased financial returns and social returns. They stressed however that the need to create return for their investors is their primary aim.

"If you screen your investments for ESG issues, then you are likely to make better investment decisions, the company you invest in will perform better, and you as a private equity house will perform better."

Another important driver mentioned was the importance of a good fit between the private equity firm and a potential company. Interestingly, the interviewees talked about smaller private companies basing their choice of buyer on private equity firms' values, competencies and industry knowledge. Mirroring this finding, the private equity firms themselves indicate that they are looking for investment opportunities where their own values are reflected in the management. A sustainability focus were highlighted as a route to create proprietary deal flow.

"In the private equity industry, we have for a while seen been bigger and bigger deals (...) the trend is now to increasingly target smaller and midsize companies. And to get the foot in the door with the smaller and medium sized companies, that are often family owned, you have to have a different approach. Those companies typically want to have smaller managers investing, who are speaking their language."

Investors pressuring for ESG activity is a notable motivational factor. Elements the interviewees point out is that investors care about private equity's ESG management, including how they are controlling risk, how they can outperform and how they can impact society through ESG activities.

"It is increasingly important to many of the big institutional investors to invest to solve some of the societal challenges we are facing."

Another element considered important by the interviewees is to attract talent to their company. Here, their ESG efforts were often highlighted as contributory factor. Interviewees talk about appreciation of their sustainability focus and ESG efforts, and of new recruits identifying themselves with the private equity firms' cultures and values.

RQ4: ESG AND COMPANY OPERATIONS

How is ESG integration reflected in Nordic PE company operations and approaches to value creation?

The integration of ESG considerations in company operations is a rather complex phenomenon to study, and my research largely relies on individual's beliefs and experiences. Looking first at the survey, I developed a set of statements which respondents were to respond to on a scale from *Do not agree* and *No opinion*, to *Strongly agree.* The figure below illustrates the GPs views. (All 60 GPs completed this section of the survey. I have excluded the responses stating "No opinion".)

Figure 33: ESG activities in relation to company culture

Interpreting "agreement" as the cumulated score of the responses *Strongly agree*, *Agree* and *Somewhat agree*, we see that most of the statements receive a high score of "agreement". However, to avoid including responses that does not explicitly agree with the statements, I'm not considering responses of "*Somewhat Agree*" in my further analysis of "agreement". I find that 80% of GPs thinks it is beneficial that employees have knowledge on ESG issues. Another 80% states that it is important that for their company to be perceived as taking ESG seriously. 77% state that their company culture welcomes ESG considerations, 63% say that their top management show a strong commitment to ESG practices and 55% say that ESG activities are becoming increasingly fundamental to company operations. Turning the focus towards employees, 48% claim that ESG activities are important for the identity and purpose of our employees and 25% that ESG activities increases creativity and innovation in their team. Finally, 18 % indicate that junior employees and job-seekers are pushing for ESG action.

Findings from the interviews

A few of the interview questions were intended to examine company operations with respect to company culture characteristics and views on value creation. I asked the interviewees for thoughts on the trend uncovered in recent research concerning ESG management moving away from being "compliance oriented" and towards becoming more "core" to company operations. Further I enquired about ESG commitment from their top management, and thoughts on the impact ESG management has had on their company culture. Also, I asked them to elaborate on how private equity firms can combine a performance culture with a culture promoting ESG and sustainability. As for the findings related to the previous research question, GPs commented on operations and value creation when answering other questions in addition to those mentioned here. Listed below are themes that commonly appeared. The full responses related to the themes are found in the appendix, chapter 8.3.

Presented with the question about the standing ESG has in the firms, defining for most of the answers, were an understanding that ESG is no longer an add-on to the investment process, or a "tick the box" activity. The interviews gave accounts of ESG moving into the DNA of the firms, being the sensible thing to do and becoming prerequisite of doing business in the first place.

"There is a movement toward ESG being part of the DNA of the companies, rather than a "tick the box" activity. I think that what's happening is that ESG becoming a part of how people do business in general, something that makes common sense to do."

Being compliant to laws and regulations is still critical for the firms, something they must do. However, the interviewees indicate that their firms are moving beyond the minimum requirements regarding compliance and reporting, and are viewing integration of ESG increasingly as a source of creativity and competitive advantage. The firms are increasingly looking for opportunities to make ESG related valuable changes to their investments, rather than applying negative screening and possibly miss out on good investments. The firms claim it is important to always consider the risk situation versus the opportunities inherent in the possible investments. When asking about the commitment on ESG issues from top management, the interviewees told of strong top management buy-in's. Top managers are believing that ESG management is something the company needs to do and should do, and this tone is moving down into the organizations.

"We have moved away from using exclusion criteria and toward seeing opportunities. For example, we bought a company a few years ago. Through Due Diligence, we found an ESG concern. Instead of saying no, we looked for opportunities. If we had just been focusing on exclusion criteria, we might not have gone through with the investment. It ended up being a very strong investment for us and our investors, in addition to the local community."

"ESG in a firm like ours starts with the tone from the top. All the way from recruitment, through new hire onboarding to new investment processes, the tone from the top is very clear communicating that ESG is an integral part of our business."

Interview findings indicate that values related to working with ESG and responsibilities for ESG are shared within the organizations. Interviewees say that working with ESG is something that resonates within the firm, commenting that "*everyone in our company believe that this (ESG) is the way we will outperform other firms"* or that *"Compliance and risk management are hygiene factors for us (...) it it is something that everybody understands that we need to work on."*. Reflecting this, interviewees noted the importance of a "sustainability mindset" permeating the organizations (see quote above to the right), and that ESG responsibilities are not treated as an an add-on to business operations, but are integrated into the responsibilities of the employees working with investments. Similarly, interviewees speak of company values relating to ESG stemming from top management buy-in as being visible all the way from the recruitment process.

"Investment strategy heads have appointed ambassadors in each of their areas to make sure that we integrate this "sustainability mindset" into the organization, so that its not just the responsibility of the responsible investment team."

"We spend significant time focusing on our values in our recruitment processes (...) that way you hire people that continues on to "live" the values and the culture that we have, and ESG is an integral part of that."

While the interviewees talk about ESG being highly integrated in the companies; becoming a hygiene factor and part of company DNA, they clearly stress that it is within portfolio companies ESG activities can have the largest impact. Noted is the differences in scale. Where private equity teams and firms are usually small, companies invested in are significantly bigger and have many more employees, ensuring a larger degree of impact from ESG efforts. However, as one interviewee noted, it is important not to ignore the effect ESG activities can have within the private equity firms as well.

"We believe in "leading by example". We recognize that it is through portfolio companies we can make the greatest impact, but it is critical that we lead by example as a firm as well."

A final comment can be made on interviewee companies ESG management among investments. They tell of ESG managed being applied in a practical and flexible way. One of the interviewees comment that ESG management becoming "core" to portfolio company operations is company dependent and that it has to be a company where it is necessary for them to focus on such issues; where it is already part of their DNA.

RQ5: THE FUTURE OF PRIVATE EQUITY

What will characterize the future role of the Nordic PE industry with respect to achieving social and environmental objectives?

Similar to the research on operations and culture, I developed a set of statements which respondents were to respond to on a scale from *Do not agree* and *No opinion*, to *Strongly agree.* The figure below illustrates the GPs views. (All 60 GPs completed this section of the survey. I have excluded the responses stating "No opinion".)

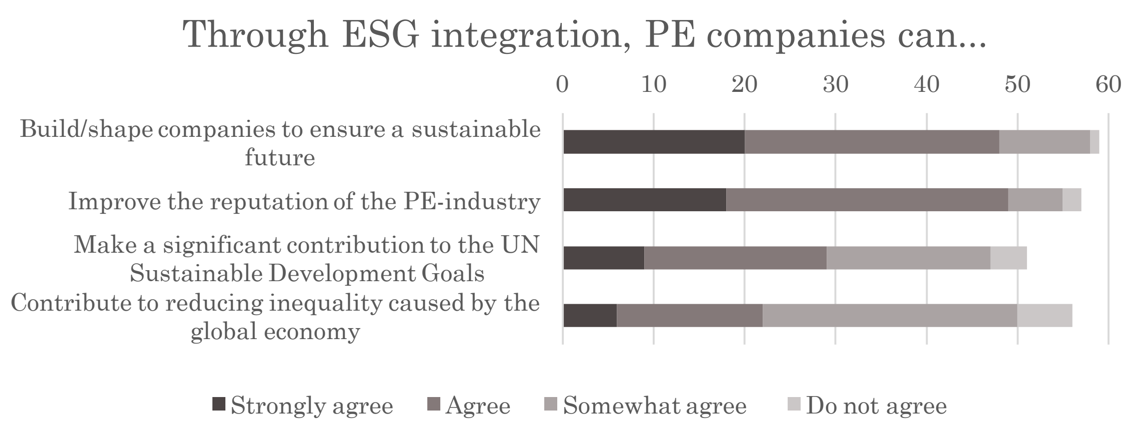


Figure 34: ESG activities and future beliefs

Again, most statements receive a high score on "agreement" when regarding it as the cumulated score of the responses *Strongly agree*, *Agree* and *Somewhat agree*. In this analysis however, I'm adopting a more conservative attitude, and do not include responses of "*Somewhat Agree*" in accounting for "agreement". I find that 80% believe that PE through ESG integration can build/shape companies to ensure a sustainable future. 82% of the GPs state that PE companies through ESG integration can improve the reputation of the PE industry. 48% believe PE can make a significant contribution to towards the UN Sustainable development goals, and a final 37% believe that PE through ESG integration can contribute to reducing inequality caused by the global economy.

Findings from the interviews

To answer this research question, I asked the interviewees to elaborate on what the industry will look like in the future with the Millennials in charge, and followed up with questions when they started talking about PE's future role in relation to sustainability. Listed below are themes that emerged from this specific question, as well as comments on future trends uncovered in their answers to other questions. The full responses related to the themes are found in the appendix, chapter 8.3.

Interviewees see Future private equity as being able to measure performance as more than just financial performance, and hope that the industry will be able to combine a long term view on company development and an appetite for change and innovation.

"We need to become much more systematic and develop measures so that we can prove in quantitative terms how our philosophy is translating into real impact, and not just tell nice qualitative stories."

Another important area concerned the people in future private equity. Overall, interviewees tell of the younger generations as being more driven by purpose, being more broadly interested in society and valuing building strong companies over delivering shareholder returns. Interviewees also talk of traits needed among future employees, including being smart, driven, humble, curious, having an entrepreneurial spirit and a passion for developing people and companies. One of the interviewees stressed that the millennium generation is much more versed in the new technology many of their new investments have to do with, and another interviewee followed up by noting that this will come naturally for the future employees.

"The people-element in the ESG agenda is very important. To move at the pace which we need to be moving, we need people with very high drive and a sense of urgency. Private equity is the perfect combination of having a long term perspective and having people who are extremely driven and wanting things to happen now, and not tomorrow."

"The challenge is to make everyone understand how sustainability and ESG can contribute to each specific company's strategy and performance."

Further education of employees on ESG matters is mentioned, with interviewees noting that there is a challenge with making everyone in the firm understand the benefits of working with ESG and sustainability. Flexibility in work routines is further stressed, being able to switch between different operational roles within PE in order to gain the broader outlook. An important factor also mentioned is the need for change in recruitment strategies. How firms man their boards and internal organization need to reflect the changed face of the business world. Diversity both in gender and in background were highlighted. However, one of the interviewees commented on a challenge we might see in recruitment going forward. The younger generations prefer to work less and have more flexibility than they might get in private equity, where they would need to "roll up their sleeves" in order to create return.

"I think that the private equity industry by nature is a bit narrow-minded. I think it is important that the industry gets more oriented towards the outer society, take part in discussions, and also take the responsibility that it is to create more sustainable companies. And I hope that Millennials will somehow answer that."

Often highlighted is the change regarding "*finding the companies of the future*". Interviewees' answers reflect the previous finding about the changing mindset on sourcing based on opportunities rather than negative exclusion. Beliefs include that the firms that are making superior returns in the future will choose their investments differently, by "*investing in companies governed by different principles*". As an example, one interviewee noted that potential benefits and solutions (for example waste reduction or resource efficiency) would be found by targeting companies having problems with such issues in the first place. Summing up, one interviewee commented on private equity responsibility to create the sustainable companies of the future (see quote).

5. DISCUSSION

The aim of my thesis has been to give a comprehensive exposition of the state of affairs and cutting edge trends on the integration of ESG issues in the Nordic private equity industry, in order to provide industry agents with an understanding of industry best practice. With this intent in mind, I developed five research questions highlighting different aspects of integration and trends. To answer my research question, I conducted an online survey where 60 General Partners provided an account for their activities and beliefs concerning ESG integration. Moreover, five semi-structured interviews were held with representatives from Nordic private equity firms, providing deeper insights into the research questions investigating motivations, organizational changes and future beliefs. Based on my understanding of the results obtained, in this chapter I will guide the reader through a discussion on prominent findings from chapter 4. I begin with looking more generally at the findings, at elements such as strategies adopted and frameworks used. I proceed to discuss the weight put on the different E, S and G issues and the industry drivers and obstacles. I spend most time discussing the findings in light of the overall organizational changes the survey and interview participants accounted for. Here I also present a conceptualization of different approaches to ESG integration. Finally make some attempts at describing what private equity might look like in the future.

5.1. DISCUSSION ON THE FINDINGS

As a backdrop, I obtained a sample consisting of private equity firms from all of the Nordic countries except Greenland. The sample represented a response rate of 25.53%, an acceptable rate compared to rates from similar research (See chapter 3.2.2. *Survey*). Notably, the firms responding can be characterized as “smaller”. I suggest keeping this in mind when contemplating the specific findings. As I’m discussing and drawing conclusions, mind also the differences between the different types of data and the consequent impact on the strength of the conclusions. Especially, bear in mind that the findings from the interviews may reflect that the group of interviewees represent PE firms particularly appreciative toward ESG. For a more detailed account of survey limitations, see chapter 6.3. *Survey Limitations and Suggestions for Further Research*.

Looking with a bird’s eye at the results from the Nordic countries, it appears to be a high acknowledgement of ESG and SRI practices. 90% are stating that ESG is an important part of their agenda (agree or somewhat agree) and 83% have, or are developing a policy for socially responsible investments. The extent of ESG integration in both the investment processes and internal organization further seem to reflect a general appreciation for responsible practices throughout Nordic PE firms. While developments among firms vary, such developments hints that the region have some cultural characteristics that are particularly appreciative of non-financial aims (see further comments in 5.1.3. *ESG adoption in the Nordic countries*). A wide range of frameworks and guidelines aid Nordic PE firms in setting, implementing and reporting on ESG objectives, including most prominently the UN PRI, UN Global Compact, Invest Europe and various national associations. Regarding possible financial and social consequences that may result from ESG activities, Nordic countries are making an effort when it comes to measurements, and indicate a will to develop procedures for obtaining quantifiable information. Reflecting an increasingly competitive market in a changing macroeconomic landscape (see chapter 2.1.2. *Development of private equity*), Nordic PE seems to be stepping up their game. Interesting to note however, is that 58 of the 60 firms believe their ESG performance is ether average or above the average of companies in the Nordic countries. This can be an indicator that the firms are not sufficiently updated on how far their peers have come on ESG integration.

5.1.1. HOW IS ESG UNDERSTOOD?

The first research question looked into what Nordic private equity firms see as the most important issues within the more general E, S and G categories (see figure 11: *Importance of specific ESG issues in investments*). As the understanding of ESG in financial markets and in private equity varies, I wanted to find out whether some specific issues were more common to consider in investments than other. As the results show, Environmental and Governance issues received higher scores, indicating stronger coherence among Nordic GPs on these issues. Notable issues include *Climate Change, Energy Efficiency* and *Air and Water Pollution* (environment), *Product Safety and Liability* and *Human Rights* (social) and *Business Ethics* and *Bribery and Corruption* (governance).

"We want to see our companies paying attention to any kind of governance issue. We have rules for how we govern the boards and how we govern the companies we invest in."

Looking at the relative importance GPs assign the different issues, out of the 55 positive responses to this question, 56% of Nordic GPs gave Governance issues top priority, whereas 25% gave Environmental and 19% gave Social issues top priority. My GP findings from the Nordic countries correspond with findings from PwC (2013) showing that 86% of private equity firms monitor governance issues in their investments, 80% monitor environmental issues and 76% social issues. PwC (2015) further looked into LP preferences, and showed that they focus more on governance than social or environmental issues, and this may reflect onto the GPs. PwC commented that this is perhaps because the link between governance and value is clearest (for example seen by the value destruction risk in companies poorly governed). Conversely, environmental and social issues are arguably understood more in terms of stakeholder value.

Interestingly, we see a pattern of the different ESG issues prioritized as a function of investor type. Governance issues prevail as top priority, but where buyout funds prioritize Social issues over Environmental issues, it is the other way around for venture and growth capital. With growth funds, we also see that Environmental issues are almost also catching up with Governance issues. While the sample of the different investor types is not especially large (28 accounts for buyout, 21 for venture capital and 16 for growth funds), the different views of the importance of Social and Environmental issues are interesting. An explanation may lie with buyout funds targeting mature industries in existing markets, where social issues, such as labour standards and product safety and liabilities (two of the most important social issue for buyout funds) are more urgent. Conversely, venture and growth funds are targeting younger and more innovative companies, or companies restructuring or entering new markets. There, the need to make sure new operations are permissible from an environmental perspective may be more urgent (air and water pollution and energy efficiency being among the most important environmental issues for venture and growth funds).

5.1.2. STRATEGIC DRIVERS

The survey results confirm that 67% of respondents focus on ESG to ensure their long term success. Illustrating, uncovered in the interviews were the GP belief that to survive in the future, PE firms must focus on ESG (see quote to the right).

"In private equity, if you ignore ESG issues, you risk your own peril."

Looking at GPs motivations for ESG management from external sources, my findings showing that most GPs view investor pressure as the most important driver, followed by public and regulatory/governmental pressure. This finding strongly corresponds with findings from previous research, including London Business School (2015) stating that investors are leading the pressure, followed by public and regulatory pressure, and both UNPRI and Mercer highlighting that fund manager selection being increasingly impacted by GPs ESG performance (see chapter 2.3.2. *Drivers of ESG & SRI*).

When it comes to internal motivations for pursuing ESG, *Financial returns* are most often listed as the main driver, followed by *Differentiation to raise funds* and *Risk management*. Interestingly, this finding is contrasting both PwC's 2013 finding placing Risk management as the primary driver of GPs ESG management and Malk finding that risk mitigation is the number one driver of ESG management (see chapter 2.3.2). Looking at the cumulative scores however, Risk management stands out, indicating that for more of the investors, internal motivations *include* risk management. This finding corresponds well with CDC Group's comment that ESG activities aiming at obtaining financial results should "*be built on effective ESG risk management*" (The Business Case, n.d.). Important to note is that the option of *Doing the right thing* or similar normative drivers is not common to find in research looking into drivers of ESG in private equity (see chapter 2.3.2.). An exception is PwC's 2013 report listing "Corporate values" as fourth in drivers of ESG in private equity. Looking at internal drivers for pursuing ESG, I chose to include this option as it would provide additional insights on investors' normative motivations, and I surprisingly found investors indicating that *Doing the right thing* is motivating them to engage in ESG to almost the exact extent as *Risk management*.

When it comes to obstacles, GPs indicate that the main one is that there are more important priorities, followed by challenges with portfolio company management (not seeing value in ESG) and data collection. Data collection being difficult and costly corroborates EY's comment on the future of private equity (2016), stating that a challenge going forward will be to understand and adopt technological solutions and master data collection and management techniques.

5.1.3. INTEGRATION IN COMPANY OPERATIONS

Indications on changes regarding company operations comes from various questions asked throughout the survey and interviews. Findings notably allow a separation into two main and closely related characteristics of company operations, (corresponding to literature found in chapter 2.3.4. *Dynamics and Future Trends*). First, ESG shows signs of becoming integral to company operations; becoming a hygiene factor and part of company DNA. Secondly and closely related are signs of changes with regards to GPs views on ESG management; from a compliance oriented activity associated with negative screening, to becoming a more proactive strategy, with deal sourcing based on opportunity for value creation and the creation of competitive advantages. Reflected in both the survey and the interviews, both developments appear to be interconnected with a changes relating to company culture.

ESG is becoming more fundamental to company operations

As noted, 90% of the survey respondents stated that ESG is an important part of their agenda (agreeing or somewhat agreeing). Problematizing different aspects of company operations (Results, RQ4), 55% say that ESG activities are becoming increasingly fundamental to company operations. (Mind, this is a conservative estimate. Including respondents answering "Somewhat agree", the percentage is 97). Interviewees strongly support this finding when they claim that ESG is becoming "*a part of how people do business in general, something that makes common sense to do"*. The views of Nordic GPs are thus reflecting wider private equity trends. To quote ERM Principal Consultant Tim van der Weide, there is an "*ongoing shift from seeing sustainability as compliance-and legacy driven to a strategic advantage that is central to a company's business model* (Weide, 2016). 63% of survey respondents say that their top management show a strong commitment to ESG practices, and interviewees contributes to this finding by telling of strong top management buy-in on ESG issues and the tone from the top resonating through the organization. The question of where the responsibilities for ESG lie within the organization can further indicate the importance ESG has within the firm. The 2015 LBS report found that ESG *policy setting* were commonly set at the board level. Reflecting that ESG considerations have taken place on the highest levels of decision-making, one firm interviewed commented that their Partner team consider ESG risks the same way they would consider any other risk type related to their investments (see appendix chapter 8.3.). In the survey, I further found that 65% of the firms assign ESG responsibilities to investment professionals and managing partners, suggesting that ESG is included in their routines working with investments, and is not some add-on compliance activity. (Mind however that most firms surveyed are quite small, and that might reflect in most teams not being able to have designated ESG staff.) Another element that may shed light on ESG taking place in company DNA is the way the survey companies relate to the UN Sustainable Development Goals. 5 out of the 60 firms claim to use the goals as guidelines in their work with ESG, but when looking at measurement procedures, 10 firms say they assess the impact their ESG activities have on the SDGs. As such measurements are not a requisite, these findings may indicate that Nordic GPs are going beyond regulatory and/or investors requirements when it comes to ESG.

ESG management is becoming a value-add for GPs

Findings from ERM (2015) and Malk (2015) mentioned in chapter 2.3.4. *Dynamics and Future Trends,* show that GPs are increasingly approaching ESG as a means for value creation, rather than a means for value protection. Findings from the survey and especially findings from the GPs interviews indicate that Nordic PE is moving in the same directions. As one interviewee concluded "*By being in tune with society, you will have a much better feeling for what will be a good investment.*" When asked about ESG strategies adopted, 73% of the firms reported that they apply negative screening and 43% of the firms reported that they apply positive screening (firms were allowed to tick off more than one strategy). Actively searching for and working with companies that may present value creating opportunities indicate a shift to what Forbes contributor Kevin Mahn named the "new SRI", characterized by investment managers considering ESG factors in a more proactive way (Mahn, 2016). The recently mentioned finding from the survey concerning internal drivers further adds to the trend, with financial results more often than risk management being reported as the main internal driver for ESG integration. Moreover, when survey respondents were asked about the importance of ESG considerations in the different investment phases, Due Diligence and Ownership/Board follow-up scored higher than Exit. This finding is similar to London Business School's (2015) findings on the same question. LBS interpret this to mean that ESG is a part of the value creating strategy, rather than some "window-dressing" activity engaged in when portfolio companies are prepared for sale. LBS further conclude that this finding corresponds with ESG responsibilities placed with investment personnel, also confirmed in my results. According to law firm White and case, firms are showing these signs of changing how they work with portfolio companies to adapt to the changing business landscape as mentioned especially in chapter 2.1.2. *Development of Private Equity.* They charge this to "*high valuations that have significantly raised the hurdle for profitability of portfolio companies"* (Johansson, Pettersson & Wireklint, 2016).

Digging a little deeper into the specifics of the value creation processes, I found that the materiality approach has a foothold (chapter 2.2.1). 63% are measuring their investments on non-financial KPIs on parts of or on their entire portfolio, and 85% are making material assessments on ESG concerns on parts of or on their entire portfolio. As ERM noted, 70% of investors have seen ESG issues as having material impact on their portfolio companies. While this finding is based on General Partners and Limited Partners surveyed worldwide, it seems Nordic PE lie ahead on materiality considerations, or are at least mirroring the current focus on materiality within private equity. When it comes to successfully measuring the impact ESG activities have on financial returns however, I found only one Nordic firm reporting to successfully measure the financial impact, but that 12 firms (20%) are developing procedures for doing so. These numbers are slightly more pessimistic than recent numbers found in the 2016 UNPRI Report on progress, where 14% report that they have been able to quantify ESG impact on financial performance. Finally, survey participants confirm that the private equity firms are addressing ESG in their investments on a company-by-company basis rather than uniformly, with 29 firms (69%) developing KPIs on a company-by-company basis. This finding is in line with the recent finding by Malk (2015), stating that ESG management processes are increasingly dependent on the different material ESG issues identified within each investment (See chapter 2.2.4.).

Illustrating both operational changes and the changing views on value creation, is the changing face of deal sourcing. From the interviews, firms talk about being the "preferred buyer". They experience that the management of potential investments (and this especially goes for family owned businesses) appreciate the private equity firm's values, that they "speak their language" and that they can contribute with valuable tools and networks. Firms on the other hand, increasingly seek out companies with likeminded people are sharing similar outlook. This they claim results value creation through making better deals, as they get to know their companies better.

Company culture

Changes in company operations and views on value creation is closely related to company culture. 77% of the firms surveyed agrees that their company culture welcomes ESG considerations. Interview participants elaborate on this stating that the performance culture of private equity firms goes hand in hand with a culture promoting ESG and sustainability. As one interviewee confirmed; "*ESG starts with culture and values, and that has been the building blocks all the way from the beginning".*

Looking back to the theoretical contributions, it is stressed that for ESG integration to be successful, managing ESG concerns in *investments* is not enough, the engagement must be "deeper" (ERM, 2016), being integrated into "organization *culture, structure and governance*" (UNPRI, 2014). During the interviews, the interviewees spoke of various characteristics of their company culture that is related to working with ESG. These findings may give an indication of what this "deeper" integration means. In the following, I present some findings from the survey and interviews that might point to various characteristics of companies that are not merely "talking", but are obtaining both strong financial AND social returns.

Interviewees spoke of shared values when it comes to ESG; with everyone in the firm believing that ESG is the way they will outperform. Higher engagement is further highlighted, both within the private equity firm and in relation to portfolio companies. One interviewee mentioned that they would earlier only engage with the CEO and CFO's in the portfolio company management. Today however, the interviewee said that there are more interaction points, for example in engaging with quality managers, environmental managers and communication people, and that this engagement is important for creating good companies. Moreover, trust is key. Exemplified, one interviewee spoke of ESG as being more a matter of trust than something that has to be incentivized. The firm trusts that the companies they invest in are performing well on ESG matters. Diversity is also mentioned by various interviewees, the importance of hiring people from diverse backgrounds and with diverse capabilities. This finding especially confirm the argument by law firm White & Case that in the current tough investment climate, stating that PE needs to "*build industry expertise to ensure they maximize the value of their portfolio companies*". They especially talk about hiring expertize with knowledge of different industries (Johansson, Pettersson & Wireklint, 2016). Another element that appeared both in the survey and the interviews were the element of creativity. One interviewee noted that "*Working with ESG, we have become smarter and more creative as an investment organization."*. As indicated by the quote above, taking ESG management to the next level, may cause excitement and spirit among employees. Comparing interviews with survey findings (conservatively analysed), I found that 25% claimed ESG activities increases creativity and innovation in their team. The interviewees further account for young talents being naturally inclined to search for purposes beyond financial returns, and they point to their company cultures and values as factors attracting new employees to their firms. A slight share of survey respondents confirmed this, with a conservative 18 % indicating that junior employees and job-seekers are pushing for ESG action. Last but not least, the interviewees account for employees experiencing proudness by being part of "something bigger", and not surprisingly, this is especially true for young talents they claimed. The

"Compliance is critical and a hygiene factor, but it doesn't necessarily drive the same level of excitement and innovation as more voluntary initiatives, where you are allowed to be more creative and think outside the box".

survey results confirm this to a larger extent, with a conservative 48% stating that ESG activities are important for the identity and purpose of employees.

Nordic culture and ESG

Characteristics of firm culture is key to understand the different management styles adopted in private equity, whether it is a culture centred around returns, financial incentives or sustainable practices. As Matten and Moon (2008) as well as Hofstede (2010) commented, countries differ on cultural characteristics. Research on the cultural characteristics of the Nordic countries found the region to be more feminine and collectivistic, with less power distance and uncertainty avoidance (Hofstede, 1980; 2010). The region values things such as equality, quality of life and a welfare societal ideal. It appears that such characteristics are reflected in the companies surveyed and interviewed, and these attributes may reflect the region's earlier and extensive adoption of ESG practice. Thus, the theoretical features of Nordic countries, along with the attributed valued by Nordic PE firms (see the section above), may imply that the previously mentioned principal-agent theory (with its focus of effectively providing shareholder returns through financial incentives) does not reflect Nordic values and operational traditions.

A stylized typology of firms' approaches to ESG

Below I have briefly summarized the different characteristics found in the survey responses and interviews regarding approaches to ESG integration. The conceptualization is not a direct outcome of my findings, but illustrate some common features of firms' ESG adoption. It is thus a model that might clarify the differences between the actors and the diversity in practices adopted. Mind that the different "stages" are highly interconnected and does not illustrate a given path. Firms may adopt a value creating strategy without putting much weight on negative screening to begin with for example. Key takeout's (as implied through my findings), is that while all firms have to consider their licence to operate, some firms are moving beyond "compliance" and toward an appreciation of ESG management as a means for both financial results and social impacts.

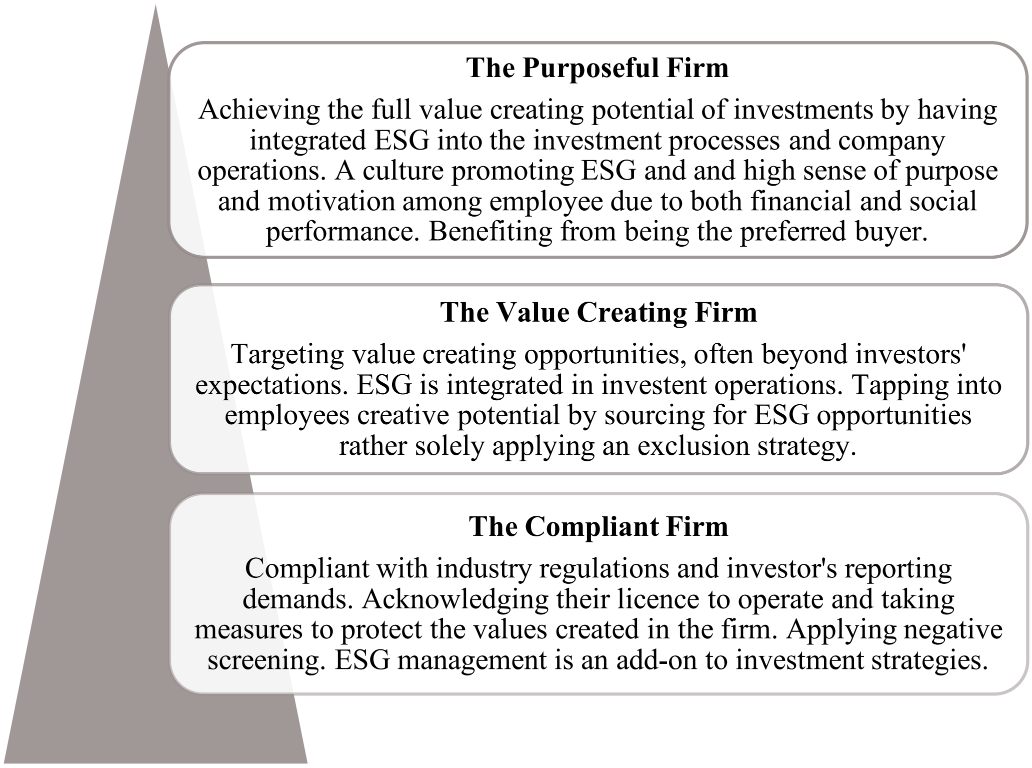


Figure 35: A stylized typology of firms' approaches to ESG

In developing this model, I have been inspired by Mr. Reynir Indahl's strategic philosophy regarding ESG integration. It might prove interesting to further research firms' level of ESG integration and develop an empirically grounded conceptualization.

5.1.4. THE FUTURE OF PRIVATE EQUITY

Where do private equity firms see themselves in the future? Which firms will prosper in the changing investment landscape? As noted, the financial landscape is characterized by increasing macroeconomic pressures. Going forward, the private equity industry will arguably experience a more competitive market where they have to actively engage with portfolio companies to a greater degree to secure sufficient returns. On the basis of findings from the survey and the semi-structured interviews, I will try to give an account for what a future private equity firm might look like. Moreover, I will try to map industry insiders' beliefs regarding PE's ability to contribute to a sustainable future.

"The financial community and the private equity community especially is gearing up. There is more and more traction within the industry in the area of combining ESG and sustainability with performance."

Future PE firms

The industry itself believes that private equity will increase its bids when it comes to ESG and sustainability. 82% of GPs believe the ESG focus among investors to have increased three years from now, supporting Malk's 2015 finding. Further they believe (to varying degrees) that investors will require PE to have a verbalized ESG policy, commit to industry standards and showing evidence on financial and social performance. Mirroring these beliefs, 75% of the firms expect their own resource allocation to increase. As discussed in chapter 2.3.2. and 2.3.3, the 2015 UNPRI report concluding that fiduciary duties are not an obstacle to ESG integration, may also impact the workings of PE going forward. Seeing as the firms believe the focus on ESG is going to increase, it is interesting to see both in the survey and in the interviews how GPs value knowledge of ESG and sustainability in their employees. 80% of GPs finds it beneficial that employees have knowledge on ESG issues, and in the interviewees, it is commented that the challenge is to educate all employees on how sustainability and ESG contributes to performance. Interview findings note that future PE will have to become better at measuring the impact of their ESG activities, as not only be able to *"tell nice qualitative stories",* but to have something quantitative to show. Attracting people with new and different skill sets as highlighted in the literature (EY, 2016), is largely confirmed in the interviews, confirming the need to further diversify and educate their employees.

The importance of being reputable

Nordic private equity companies place high importance on being seen as taking their ESG responsibilities seriously, with 80% agreeing or strongly agreeing with the statement. This finding indicate that the industry place weight on being and becoming reputable. As EQT Managing Partner Thomas von Koch stated "*success is not about becoming the biggest firm, but the most reputable"*, and in his 2016 article, he talks about successful future GPs having to do business in a reputable way, making them the preferred buyer of both managers in prospective acquisitions and investors. Interview findings corroborate Mr. Koch's visions, by participants speaking of being chosen by prospective companies because of their culture, values and the diverse tools and networks they can contribute with. Survey findings largely indicate that Nordic private equity firms value being reputable, as 82% of GPs report that PE can improve the reputation of the industry through ESG integration.

PE as a social agent

The previously mentioned inherent characteristics of GPs (being creative, driven and having both a long term perspective and a sense of urgency) was mentioned by one of the interviewees as the perfect combination to *"move at the pace which we need to be moving"* regarding the creation of sustainable future companies. While this is the view of one GP, it seems the Nordic GPs in general share similar thoughts. As active managers and owners of private companies, GPs are part of the society. This role seems to be understood by many GPs. Seen in the survey results, 80% of GPs believe that PE through ESG integration can build/shape companies to ensure a sustainable future. As earlier displayed in a quote, an interviewee confirmed this by stating that "*it is important that the industry gets more oriented towards the outer society, take part in discussions, and also take the responsibility that it is to create more sustainable companies."* Further, as many as 48% say that PE through ESG integration can make a significant contribution to towards the UN Sustainable development goals, and finally 37% believe that PE can contribute to reducing inequality caused by the global economy. To sum it up, findings indicate that Nordic PE is increasingly viewing ESG management as a tool for value creation and a means competitive advantage, and this trend may benefit both the firms themselves and society at large.

"There is only so much a few people can do, and if we want this to move at scale, it needs to be part of people's everyday work. Society, the financial industry, the private equity industry, EQT – we are all on a journey. We need to learn to speak the same language, see the opportunities the sustainability agenda brings and continue to push for positive change."

6. CONCLUSIONS

In this chapter, I will conclude my findings. Moreover, I will look into possible managerial and theoretical implications before I finalize by giving an account of limitations with my thesis and directions for further research.

6.1. CONCLUSION

In my thesis, I wanted to look into ESG (Environmental, Social and Governance) integration in private equity, an area scarcely researched. As a frame, I chose to target the Nordic private equity industry (defined as firms headquartered in the Nordic region), and based on findings I wanted to provide an overview of the extent of Nordic ESG integration as well as future trends.

Macroeconomic developments such as climate change and increasing economic inequalities are as pressuring, the competition is high among private equity firms to secure the best deals and the industry is increasingly being regulated and held liable for irresponsibilities. Such pressures have encouraged PE to step up their game in order to create returns. Turning towards sustainable operations, responsibility measures have often been viewed as unnecessary and hampering growth, imposed by outsiders on the financial industry. The change toward sustainability within private equity we see today however, is taking on different characteristics, being more a change from within. Investors are increasingly educated on the importance of effective ESG management, especially when it comes to risk management, and GPs are showing signs of taking ESG management seriously to be able to raise funds. Further, as GPs are taking on ESG activities, their appreciation for the value creation possibilities that comes with ESG is increasing.

To address the extent and development of ESG integration in Nordic PE, I formulated five research questions on cutting edge themes, and gathered data from an online survey of 60 Nordic General Partners and from semi-structured interviews with five representatives of assertive Nordic firms.

Concerning the understanding of the ESG concept, I found that Governance issues are most important among ESG issues for Nordic GPs as a whole, but that growth and venture capital firms see Environmental issues as a second, while buyout firms rank Social issues second. Among the specific issues seen as important in investments, I found *Climate Change* and *Energy Efficiency*, as well as *Business Ethics* and *Bribery and Corruption*. Looking into the extent of ESG integration in the Nordics today, I found that most firms have or are developing a policy for socially responsible investments, and that they are mostly applying negative screening strategies, but that a considerable among of firms also apply positive screening strategies. Regarding guidelines and frameworks, they are mostly aided by the UNPRI, Global Compact, EVCA and various national frameworks. ESG responsibilities are placed with investment professionals, and ESG is important in all phases of investments, but especially in due diligence and ownership. Nordic PE is showing a will to measure the financial impact of their ESG efforts, but so far measurements are mostly done by tracking material non-financial KPIs. Findings further show that they are applying a company-by-company rather than a uniform approach on all investments regarding non-financial KPIs. Giving an account for the drivers and obstacles impacting ESG integration, Investor pressure and the possibility to create additional financial returns are reported as the main strategic drivers of ESG integration. Among obstacles, main ones include that there are more important priorities to focus on, portfolio company management seeing little value in it, and that ESG data collection is costly and difficult.

Regarding company operations, most survey respondents say ESG is an important part of their agenda, and this is reflected in ESG being increasingly treated as part of the investment procedures, not just as an add-on activity. Interviewees confirm that ESG management is becoming part of how they do business in general; being the "sensible thing to do". When it comes to value creation, we are seeing changes in firms' business models, as they are moving beyond a "compliance" attitude toward viewing ESG management as a value creating strategy and a means for obtaining competitive advantage. By developing operational excellence and showcasing their values, the firms are showing signs of becoming the preferred buyer (especially when the private firms are family owned), a valued position in a highly competitive market. Importantly, a company culture embracing ESG and employees developing an "ESG mindset" is important for successfully extracting added value from ESG efforts. Substantiated by interview findings, the more successful firms seem to be benefitting from highly engaged employees finding motivation beyond financial results, that are full of purpose in being part of something bigger, and are able to convert this to value by putting their business drive into play. Concerning the future of private equity firms, Nordic PE appears to acknowledge their role in creating the sustainable companies of the future. All in all, Nordic PE is showing signs of taking their licence to operate seriously, by being worthy the time of both their investments and investors, as well as outer stakeholders.

It seems like strategies favouring ESG activities is a function of the cultural characteristics among the Nordic countries. Feminine values, equality and caring for the needy as theory assigns the Nordic countries might reflect the earlier and extensive adoption of ESG practice.

While my findings indicate a move toward extensive ESG integration, it is important to stress that as much as firms strive to perform along ESG dimensions, it is not possible to ignore the need to create returns. Without creating returns for their shareholders, PE firms have no possibilities to find and manage new companies. Further, while trends indicate a change toward targeting value creating opportunities, proper risk management cannot be ignored. As the interviewees stressed, compliance is critical. But signs largely indicate that firms are doing more. As Bob Eccles of Eurosif mentions (Eurosif, 2016), ESG integration mostly depends on whether GPs value ESG issues in their investment decisions. Evidence is building on the link between ESG integration and performance, but ultimately, integration depends on GPs priorities, being the investment fiduciaries. While the UNPRI have made a case for the inclusion of ESG in fiduciary duties, no hard laws exist, and the degree of integration stands and falls with the private equity firm.

Implications for managers include being aware of the degree of integration and best practice concerning ESG among their peers. Knowledge on the important drivers of integration in the industry might give GPs rationales for pursuing ESG. Knowledge on common obstacles to integration, may provide an indication of where to direct resources. Finally, by illuminating the perceived link between company operations, culture and value creation, managers may find reason to encourage positive changes. My thesis is further a contribution to the emerging field of research on ESG integration in the private equity industry, and particularly opens up for further research on the financial rationales for pursuing ESG, comparisons of ESG integration between asset classes and the motivational effects on employees working with ESG.

With this research, I will give a comprehensive exposition of the state of affairs and trends on the integration of ESG issues in the Nordic private equity industry.

6.2. MANAGERIAL AND THEORETICAL IMPLICATIONS

Managerial Implications

As indicated in the introduction, I wanted to provide knowledge on the extent and trends of ESG integration in the Nordic countries, and specifically General Partners operating out of Nordic countries a thorough exposition of the operations of their peers, and strategic rationales for embracing ESG in their organization and investments. The results and discussion section provides various organizational takeaways for General Partners.

Mainly I argue that it is beneficial for the GPs to have an understanding of the workings of their peers, and learn of the directions they are heading. As the business landscape is getting more competitive, it is useful to have as much information as possible that could potentially be valuable for them in their investments. For example, if firms have yet to consider ESG, it might be an important factor to focus on going forward, as the wider industry expects that investor pressure is going to increase, and particularly their selection of fund managers. Looking at it from the other side, forerunners on ESG integration may experience that this no longer constitutes an urgent and pressing matter for their investors, as they have already integrated it thoroughly into company operations and investment procedures. Important for GPs in Nordic firms to consider however, is that fact that they all believe that they are in front or averaging when it comes to their ESG efforts (see chapter 4, RQ2). Reading this thesis might shed some light on how far the Nordics have come on ESG integration, and possibly encourage the laggards to keep up with their peers.

This thesis may further illuminate how peer GPs are applying guidelines and frameworks in their setting, managing and reporting on ESG activities, and encourage GPs to increase their commitment. Knowing where peers assign the responsibilities for ESG management, and learning of the benefits of avoiding to treat ESG as an add on activity or only engaging in ESG in exit preparations, may also encourage changes in the responsibilities of operational roles.

By shedding light on the different drivers for ESG integration and the most commonly cited obstacles, this research may impact the understanding of why peer GPs focus on ESG to the extent we see today, and point to important areas to focus their attention and resources, to ensure that the integration process go as smoothly as possible. For example, for a company having hurdles with ESG integration, it may be wise to focus their efforts on rising firm awareness of ESG, teaching portfolio companies on the benefits of effective ESG integration, and spending resources on developing effective collection and analysis of ESG data. Further, seeing how peer firms value material ESG issues, and having in mind the finding from Khan, Serafeim & Yoon (2015) on the possible financial results from focusing on material ESG issues, this thesis may motivate GPs to increase their efforts to quantify the impacts of their ESG efforts.

Looking at the findings on the organizational characteristics of firms effectively creating value from ESG activities, industry agents may obtain a different understanding on the connection between ESG and value creation. For example, by seeing how elements such as a company culture and top management buy-in on ESG considerations may result in value creation, on grounds such as increased creativity and innovation, a sense of purpose, firm reputation and being preferred of management in potential investments.

Finally, GPs are presented with peer beliefs on the future possibilities that lay with private equity (having dedicated and creative people and long investment horizons and so on) in becoming an important player in creating a sustainable future. Illuminating GPs beliefs about how private equity can take part in solving for example the UN Sustainable Development Goals and contribute to reducing economic inequalities may encourage more GPs to develop a will to create positive change.

To take ESG integration to the next level within PE firms, I suggest looking into UNPRI's Guide for General Partners, a designated guide on how to implement ESG into the firms' operations and investments.

Theoretical Implications

What *the concept of ESG* means, in the sense of what the main pillars, Environment, Social and Governance include, is rarely clarified in extant literature on private equity. I have tried to address this conceptual vagueness by giving an account for what Nordic private equity firms understand of the concept. Particularly, I believe that clarity around what GPs see as important in investments can lay a path for further research on the importance the industry assign to the different issues.

By shedding light on the developments concerning *ESG integration in private equity*, I am contributing to an area that is scarcely researched. Academics working with ESG and may gain insights on how the concept fares within the private equity industry, and conversely, researchers working in the field of private equity, may gain knowledge on an emerging field impacting the industry.

Further, I have investigated private equity in the *Nordic countries* with relation to ESG integration. Previous contributions to the literature have predominantly applied a global frame, or focused on specific locations such as France, the UK or the Netherlands. I am contributing to the literature by illustrating how private equity this particular geography, often seen as a forerunner on sustainability, is rapidly embracing ESG. My findings indicate that theories of financial incentives driving motivation may need to take cultural characteristics into account.

Knowledge on the different guidelines and tools the industry is relying on in working with ESG can contribute to research on the diffusion and importance of different frameworks. I am further contributing to the literature with insights on the emerging link between the adoption by firms and individuals of an ESG mindset and value creation.

6.3. RESEARCH LIMITATIONS AND SUGGESTIONS FOR FURTHER RESEARCH

Over the course of writing this thesis, I have gained insights into the Nordic private equity Industry; into various characteristics and trends concerning ESG integration. I therefore believe that this research can add to the existing knowledge on ESG integration in private equity, especially within the Nordic area. However, there are a few areas where my research may show weaknesses and limitations.

While I have been supported by my supervisor and industry experts during the process of writing the thesis, and have tried to adopt a critical attitude, it is unquestionable that my study is impacted by me writing it alone. Another important point to stress is that I have had to rely largely on reports from industry associations, consultancies and other non-academic sources in theoretically grounding my research. As a result, there are limitations to the conclusions (see chapter 3.2.1. *Literature Review*). Viewing this in a positive light however, the field of research is new, and my research may contribute to address the gaps that lack theoretical grounding. Another point to stress is that most of the literature I have relied is very recently written, as the phenomenon is fairly new. A certain bias may stem from pioneer research showing a tendency to be more enthusiastic.

Various biases may further limit my research. Primarily, I risk self-selection biases as those who chose to respond to my survey are arguably more likely to represent firms that already have a positive attitude towards and are more competent with regards to ESG management. This bias may be even stronger in the interviews, as I based my sampling on factors such as firms showing interest in my survey, and firms communication strongly on ESG or responsibility on their websites. Consequently, the conclusions drawn may be limited. Doing interviews with General Partners representing private equity firms not having made efforts towards ESG integration or have different views on the importance of ESG could have both impacted my findings from the interviews in other directions, and have strengthened the validity of the research. Another factor to stress is the cross sectional nature of the research. Longitudinal studies provide stronger conclusions, but the time frame of my research prohibited me from taking this approach. Moreover, my thesis is limited by information biases, particularly because the information obtained in the survey has not been objectively verified and may not reflect reality as it really is. The risk of social desirability bias is especially pertinent regarding the interviews, as respondents may have been answering my questions so that it would seem to me that they are more positive to and engaged in ESG activities than they really are. Narrowing my research field to the Nordics, may also have limited the generalizability of my research to other geographical areas due to factors such as the distinct social and cultural characteristics shared by the countries, being already perceived as forerunners on sustainability issues, and technical differences such as many PE firms being considerably smaller. Adopting a descriptive research design examining the characteristics of GPs in the entire Nordic area provided me with a great deal of information. By additionally conducting exploratory research on beliefs among assertive GPs, I gained deeper insights. By doing a multiple method research, and because my time frame was limited, my analysis of the industry is only able to give an account for the main trends. If I had time to conduct more thorough case studies on the workings of the different firms, I may have been able to give more detailed results. Specifically, the thesis may have benefitted from conducting more sophisticated quantitative analyses. I argue however that by applying a mixed method model of research, the findings nevertheless gained substance and depth.

This thesis is written from a strategic angle, and I regret that I could not supply my thesis with additional empirical findings on financial characteristics (Increased ROI, ROA, IRR etc.) to back up statements and beliefs with relevant numbers. However, doing so would possibly have proved hard, both because the private equity firms themselves find it difficult to measure impacts empirically, and it would require a more lengthily and complex research process. However, I am positive that such evidence will appear in the years ahead.

The thesis' empirical setup does not demand an extensively theoretical approach. This may be reflected in the thesis' building blocks being half descriptive (survey) and half explorative (interviews), in sum representing a relatively explorative approach to the different themes. Further research may apply a more theoretical angle to the questions examined.

While I have contributed to research on ESG in private equity, and interesting area of research lies in comparing PE and public asset managers on the extent and traction of ESG integration. Further, it would be interesting to look into how different PE firms value short term profitability from ESG efforts (for example stemming from avoiding certain industries for certain periods of time) and long profitability term profitability from ESG efforts. I regret not going into this theme when conducting the survey and interviews, as it would have provided my thesis with more thorough insights on strategic ESG considerations.

My focus mainly lay on private equity firms in general and overall portfolio company investments. It would prove interesting areas of research to examine more deeply how the different asset classes manage their funds differently in relation to ESG, for example examining more thoroughly which specific ESG issues they value more and what specific ESG initiatives they have engaged in. Also interesting would be to look at whether the focus on ESG differ between funds in larger private equity firms. Whether the extent of ESG integration differ between captive funds (often owned by banks, corporations or other private equity firms) and independent funds (owned by the firm partners) differ would also be interesting. Crifo & Forget confirmed this hypothesis in their 2012 report on the French PE industry, finding that while fundraising is easier for captive funds, independent funds are more likely to develop responsible practices in order to attract investors. It would be interesting to see if this also goes for the Nordic market.

It would provide additional depth to the research if I had included questions about the position of the person responding to the survey. As ESG responsibilities are assigned to various position within the firms, the responses may have been impacted. While employees may share the same knowledge on practical matters concerning ESG such as frameworks or strategies adopted, I suggest doing more research on the on board members of the firms, to see if views and beliefs concerning ESG integration resonates within the top management of the firms.

Another suggestion for further research deals with the link between company culture and employee mindset embracing ESG and value creation within. Specifically, the impacts on creativity and innovation stemming from employee purpose and motivation. Much is written in the literature about motivation and performance in general, but I find that this link is especially interesting to research in the field of private equity, being inherently focused on creating strong companies over longer periods of time. Finally, an interesting direction for further research would include making measures to distinguish between the private equity firms that are leaders/forerunner on ESG and those that are making minimal commitments. This kind of information could prove useful for private equity firms in future fundraising.

Research on private equity per se is scarce (especially for Nordic countries), and the crossing of PE and ESG barely non-existent in theoretical research. As I have mentioned, the industry is especially tricky to get a hang of due to traditions of nondisclosure and little transparency. However, with the increased reporting requirements, and interests of other stakeholders regarding the workings of private equity, I assume that we will se a lot more research in this field going forward. To map the extent of ESG integration in private equity, this research is but a small step. I hope however that my research can provide a starting point for further research into ESG and Nordic private equity, and I'll be happy to contribute to any further research.

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8. APPENDIX

8.1. INTERVIEW GUIDE

- What are your thoughts on ESG integration as a source for competitive advantage?
- How can private equity firms combine a performance culture with a culture promoting ESG and sustainability?
- How would you describe the commitment on ESG issues from your top management?
- Can you describe some effects working with ESG has had on company culture?
- Research has found that ESG management is moving away from “compliance” and toward being “core” to company operations. How would you say that this applies to your company, and the overall Nordic PE industry?
- What is the purpose of your company? (Why are you here?)
- What will the private equity industry look like in the future with Millennials in charge?

8.2. QUESTIONNAIRE

To what extent do you agree to the statement: "ESG is an important part of our company's agenda"

- Does not apply
- Disagree
- Somewhat disagree
- Neither agree nor disagree
- Somewhat agree
- Agree

1. **Do you have a policy or established standards for Socially Responsible Investment?**
   - No
   - In development
   - Yes

2. **Please indicate which international guidelines/frameworks you apply in the integration and management of ESG?**
   - EVCA/Invest Europe
   - National Frameworks
   - PEGCC Guidelines
   - UN Global Compact
   - UN PRI
   - UN Sustainable Development Goals
   - Other
   - Does not apply

3. **Please indicate which of the following environmental issues you perceive as most important to consider in investments. You may select a maximum of five issues (or less). If you think none of them are relevant, please click "None of the above".**
   - Air and water pollution
   - Biodiversity
   - Climate change
   - Deforestation
   - Ecosystems services
   - Energy efficiency
   - Hazardous materials
   - Land degradation
   - Resource depletion
   - Waste management
   - Water scarcity
   - None of the above

4. **Please indicate which of the following social issues you perceive as most important to consider in investments. You may select a maximum of five issues (or less). If you think none of them are relevant, please click "None of the above".**
   - Customer satisfaction
   - Data protection and privacy
   - Diversity and equal opportunities
   - Employee attraction and retention
   - Employee engagement
   - Government and community relations
   - Human capital management
   - Human rights
   - Indigenous rights
   - Labour standards
   - Labour-management relations
   - Marketing communications
   - Product mis-selling
   - Product safety and liability
   - Supply chain management
   - None of the above

5. **Please indicate which of the following governance issues you perceive as most important to consider in investments. You may select a maximum of five issues (or less).   If you think none of them are relevant, please click “None of the above”.**
   - Accounting standards
   - Anti-competitive behaviour
   - Audit committee structure
   - Board composition
   - Bribery and corruption
   - Business ethics
   - Compliance
   - Executive remuneration
   - Lobbying
   - Political contributions
   - Risk management
   - Separation of chairman and CEO
   - Stakeholder dialogue
   - Succession planning
   - Whistleblower schemes
   - None of the above

6. **Please indicate the relative importance you give the different issues (environmental, social or governance) in your investments. Drag the items from the list to the box and rank. If you think none of them are important, please list “Does not apply”.**
   - Environment
   - Social
   - Governance
   - Does not apply

7. **How important are ESG considerations in your different investment phases? (If you do not consider ESG important in one or more phases, please leave the bar blank.)**
   - Due Diligence
   - Board Follow Up/Ownership
   - Exit

8. **Which of these ESG strategies do you adopt in company investments?**
   - Negative screening: e.g. alcohol/tobacco/guns/gambling or worst-in-class.
   - Positive screening: e.g. companies with strong ESG follow-up or best-in-class.
   - Does not apply

9. **Who is responsible for the implementation of your company’s socially responsible/ESG investment policy?**
   - ESG professional
   - Investment Professional
   - Managing Partner
   - COO/Head of IR
   - Other
   - Does not apply

10. **Do you agree with the following statement: "We have frequent communication regarding ESG related issues with…"**

	Does not apply	Strongly disagree	Somewhat disagree	Neither agree nor disagree	Somewhat agree	Strongly agree
Portfolio company management	❍	❍	❍	❍	❍	❍
Investors/LPs	❍	❍	❍	❍	❍	❍

11. **What do you consider to be drivers of ESG integration from outside the company? Drag items from the list to box. Choose one or more and rate:**
    - Investor pressure
    - Government/regulatory pressure
    - Public pressure
    - Peer pressure
    - Other
    - Does not apply

12. **To what extent do you consider these factors as drivers of ESG integration inside the company? (If an element is not considered, please leave the bar blank.)**
    - Risk management
    - Financial results
    - Differentiation to raise funds
    - Doing the right thing

13. **What do you perceive as the biggest obstacles to your work with ESG integration? Drag items from the list to box. Choose one or more and rate:**
    - There are more important priorities
    - Portfolio companies see limited value in it
    - Partner group disagreement regarding the importance
    - Limited knowledge of ESG frameworks
    - Unclear legislation or regulation
    - Difficult and costly collection of ESG data
    - Other
    - Does not apply

14. **In your view, how is your company's ESG performance compared to the industry average in the Nordic region?**
    - Below average
    - Average
    - Above average

15. **Three years from now, which of these elements do you think LPs will expect you to have in place**?
    - An ESG policy
    - A commitment to industry standards (UNPRI/Invest Europe etc.)
    - Integration of UN Sustainable Development Goals in company operations/vision
    - Evidence on the impact of ESG on company value
    - Evidence on the societal benefits of ESG

16. **Three years from now, do you expect the ESG focus among your investors to...**
    - Decrease
    - No change
    - Increase
    - Does not apply

17. **Three years from now, what do you expect will be your resource allocation to ESG activities (e.g. time, money, human resources)?**
    - Decreased
    - No change
    - Increased
    - Does not apply

18. Employees/team: To what extent do you agree with the following statements:

	No opinion	Do not agree	Somewhat agree	Agree	Strongly agree
It is beneficial that our employees have knowledge on ESG issues	❍	❍	❍	❍	❍
Junior employees and job-seekers are pushing for ESG action	❍	❍	❍	❍	❍
Our ESG activities increases creativity and innovation in our team	❍	❍	❍	❍	❍
Our ESG activities are important for the identity and purpose of our employees	❍	❍	❍	❍	❍

19. Company: To what extent do you agree with the following statements: "In our company..."

	No opinion	Do not agree	Somewhat agree	Agree	Strongly agree
We focus on ESG to ensure long term success	❍	❍	❍	❍	❍
Top management show a strong commitment to ESG practices	❍	❍	❍	❍	❍
ESG is becoming increasingly fundamental to our operations	❍	❍	❍	❍	❍
It is important that we are perceived as taking ESG seriously	❍	❍	❍	❍	❍
Our culture welcomes ESG considerations	❍	❍	❍	❍	❍

20. Society: To what extent do you agree with the following statements: "Through ESG integration, PE companies can..."

	No opinion	Do not agree	Somewhat agree	Agree	Strongly agree
Improve the reputation of the PE-industry	❍	❍	❍	❍	❍
Build/shape companies to ensure a sustainable future	❍	❍	❍	❍	❍
Make a significant contribution to the UN Sustainable Development Goals	❍	❍	❍	❍	❍
Contribute to reducing inequality caused by the global economy	❍	❍	❍	❍	❍

21. Do you measure non-financial KPIs related to ESG activities in your investments?
- No
- For some investments
- On the entire portfolio

22. Please describe your approach for non-financial KPIs:
- Does not apply
- We use a consistent/uniform approach for all investments
- We develop KPIs on a company-by-company basis

23. Do you consider the materiality of ESG concerns when assessing and monitoring investments?
- No
- For some investments
- For the entire portfolio

24. Do you measure how your investments contribute to the UN Sustainable Development Goals?
- No
- For some investments
- For the entire portfolio

25. Do you measure whether your ESG activities affect the financial performance of your investments?
- No
- We have tried, but we find it difficult
- We are working on developing measures
- Yes

26. How have your ESG activities impacted:

	Does not apply	Highly worsened	Somewhat worsened	Neither worse nor better	Somewhat improved	Highly improved
Company valuations	❍	❍	❍	❍	❍	❍
Risk	❍	❍	❍	❍	❍	❍

27. In which country is your company headquartered?
- Denmark
- Finland
- Greenland
- Iceland
- Norway
- Sweden

28. Amount of AUM (€)
- Under 500 Mn (€)
- 500-1000 Mn (€)
- 1-5 Bn (€)
- 5-10 Bn (€)
- More than 10 Bn (€)

29. What is your average size of investment? (€)
- 0-25 Mn (€)
- 25-50 Mn (€)
- 50-75 Mn (€)
- 75-100 Mn (€)
- Over 100 Mn (€)

30. What is the headcount of your company/PE department?
- Less than 5
- 5-10
- 10-15
- 15-20
- More than 20

31. Describe the gender composition in your company/PE department
- All female
- Mostly female
- 50/50
- Mostly male
- All male

32. Industry preferences/sectors:
- Cleantech
- Consumer
- Energy
- Generalist
- Health Care & Life
- ICT
- Industrials
- Other

33. Fund stages

- Buyout
- Funds of Funds
- Growth
- Mezzanine
- Secondaries
- Turnaround
- Venture
- Other

34. Finally, please state the name of your company: (PS. This question is only for registration purposes – the company name will not be included in the final dataset.)

8.3. FINDINGS FROM SEMI-STRUCTURED INTERVIEWS

Following are findings from the in-depth interviews. They are summarized, categorized and coded according to the research questions concerning value creation/competitive advantage, culture and future trajectories.

Key word	Topic	Quote
Motivations		
Improved investment decisions	ESG ensures better investment decisions and improved performance	*If you screen your investments for ESG issues, then you are likely to make better investment decisions, the company you invest in will perform better, and you as a private equity house will perform better.*
Improved investment decisions	Being in tune with society ensures better investment decisions.	*By being in tune with society, you will have a much better feeling for what will be a good investment.*
Preferring sellers	Preference to invest in companies with similar values	*It is important for us to invest in companies that have similar outlook as we do, where likeminded people own and run the businesses with us.*
Preferring sellers, Improved investment decisions	Getting to know the companies, and investing in those they like result in better deals.	*We go and find the companies we like, the business owners we like, and we invest. We find this results in better deals as we spend more time getting to know the management and co-owners of the companies we invest in.*
Being the preferred buyer	With the trend for smaller deals, companies, often family owned, want GPs speaking their language.	*In the private equity industry, we have for a while seen been bigger and bigger deals, and the very largest managers teaming up to do even bigger deals. With so many private equity firms competing, the trend is now to increasingly target the smaller and midsize companies. And to get the foot in the door with the smaller and medium sized companies, that are often family owned, you have to have a different approach. Those companies typically want to have smaller managers investing, who are speaking their language.*
Being the preferred buyer	Spending much time on deals and winning with lower bids because of shared values.	*We work very structured with spotting deals. For example, in our last fund, we talked to the entrepreneurs for three and a half years on average before we bought their companies. We see that we win many of the deals without offering the highest bids, and when asked about why they chose us, they often explain that our values fit well with their own.*
Being the preferred buyer	Portfolio companies appreciates firm ESG efforts, tools, networks, culture.	*We have seen that ESG impacts our brand positively when talking to prospective portfolio companies. ESG and sustainability is not what ensures that we win bidding processes, but these companies understand that we can contribute with tools and networks; that the culture we have and the judgements we make can contribute to their work on on ESG matters.*
Being the preferred buyer	Becoming the preferred buyer for example for a family business.	*Sustainability is also a source of being the preferred buyer. If you are looking to partner up with a family business for example, hopefully they will want to engage someone who is responsible and where they feel sustainability is at the core of the investment philosophy.*
Proprietary deal flow	Sustainability can create proprietary deal flow.	*Sustainability is a lens through which we can create proprietary deal flow by being very thoughtful of what will be attractive niches to invest in going forward.*
Survival	Focus on ESG or you die.	*In private equity, if you ignore ESG issues, you risk your own peril.*

Outperformance, Investor pressure	ESG ensures outperformance.	*There is a lot of commitment, and also from our investment committee, because I think everyone in our company believe that this is the way we will outperform other firms.*
Investors want ESG	ESG performance are demanded from investors.	*Controlling risk and documenting how we could take advantage of ESG related matters in our companies is something that our investors are very interested in, and we receive more and more questions about this from our investors. So I will say that it is an advantage in relation to our investors.*
Investors want ESG	Investors want to solve societal problems.	*We see that it is increasingly important to many of the big institutional investors to invest to solve some of the societal challenges we are facing. By our sustainability focus we are being a solutions provider, and also a "safe pair of hands" for investors.*
Financial returns	ESG management is important, but creating returns are more important.	*Many private equity firms, especially the bigger firms, knows that this (ESG management) is of growing importance to their business. Whether you are investing in a listed or non-listed company, as an investor you have to make sure that the assets you own are sustainable. But of course, I still think that it is most important for private equity firms to create a return, and if you need to be more sustainable to create that return, you will do it.*
Investors want ESG, Financial returns	ESG is not a competitive advantage in itself. You need to have return on top.	*Investors are measuring the GP's on net IRR. It does not help that you have a very strong ESG performance if you don't give them return. But more and more, we see that investors are taking both return and ESG into consideration. ESG integration in itself is not a competitive advantage. You need to have return on top.*
Financial returns AND social returns	Creating financial returns while positively impacting society and environment.	*Increasing research show that there is a correlation between high ESG performance and high financial returns. Our belief is that we will be able to create top decile returns through also creating positive impact from an environmental and social perspective.*
Attracting talent	Talents appreciate ESG efforts.	*When we attract talent to our company, one of the factors they like is our emphasis on ESG issues.*
Attracting talent	Culture attracts talents.	*Our culture is one of the things that make the talents come and work for us.*
Attracting talent, retaining talent	Attracting and retaining talent at firm, portfolio company and advisor level.	*A sustainability focus is critical to attract and retain talent, and create engagement on all levels; at in our firm, within portfolio companies and among advisors.*
Attracting talent	Attract people who identify with firm values	*We use the ESG message in our recruiting process. We attract people who identify themselves with our firm's culture and our values.*
Integration in operations & Cultural specifics		
Top management buy-in, Shared values	ESG buy-in from the top on strategic grounds.	*There is a lot of commitment, and also from our investment committee, because I think everyone in our company believe that this (ESG) is the way we will outperform other firms.*
Top management buy-in, Shared values	Strong tone from the top moving down in the organizations.	*Overall, the tone from the top has been really strong driving ESG and sustainability in our company, and the tone moves down into the organization. ESG is seen as something we need to and should continue to work on with our companies.*
Top management buy-in	ESG in investments supported from top management.	*We very much encourage our companies to work with these issues, and we have full support from our top management. Our top management knows that we have to address ESG related issues, and that it is important for our investors.*
Top management buy-in, DNA, Recruitment	Tone from the top. ESG is an integral part of our business.	*ESG in a firm like ours starts with the tone from the top. All the way from recruitment, through new hire onboarding to new investment processes, the tone from the top is very clear communicating that ESG is an integral part of our business.* *Our partner team is focused on ESG risk in the same way they focus on any other risk types in our investments.*
Top management buy-in, DNA, Responsibilities	Responsibilities throughout the organization, buy-in needed to convert sceptics	*Investment strategy heads have appointed ambassadors in each of their areas to make sure that we integrate this "sustainability mindset" into the organization, so that its not just the responsibility of the responsible investment team.*

DNA	A competitive culture is good, but ESG and a performance culture go hand in hand.	*There should be a competitive culture in private equity, but ESG should be directly linked to the values and the culture you build in your firm. We don't see having a performance culture versus a culture promoting ESG as opposite goals. Is goes hand in hand. If you do ESG right, you lower your risk situation and increase value creation.*
DNA, Shared values	ESG is the sensible way to do business.	*We do it top-down in the sense that the senior people within our company buy into ESG being the sensible way to do business.* *I think that what's happening is that ESG becoming a part of how people do business in general, something that makes common sense to do.*
DNA	ESG is more than "tick the box".	*There is a movement toward ESG being part of the DNA of the companies, rather than a "tick the box" activity.*
DNA, Trust	ESG is more a matter of trust than something incentivized.	*We don't necessarily have some sort of an incentive scheme, but we definitely trust the ESG performance of our companies that we are investing in.*
DNA	ESG is the DNA.	*The ESG focus is the DNA of our company.*
DNA, Responsibilities	ESG is integrated, not an add-on.	*ESG considerations is an integral part of our investment processes, and we have clear decision gates from top management. ESG is not something we do as an add-on to our business operations. When we look at investments, we do not have a situation where an ESG team works as an addition to the deals team. If we find issues in Due Diligence, we can for example use environmental consultants if needed. But the responsibility for ESG is placed with the deals team.*
DNA, Compliance	Compliance and risk management has become hygiene factors.	*Compliance and risk management are hygiene factors for us. It is not something that is being "placed" in all our companies, but it is something that everybody understands that we need to work on and a prerequisite to do business in the first place.*
Compliance, Creativity	Compliance is needed, but does not create drive and creativity.	*Compliance is critical and a hygiene factor, but it doesn't necessarily drive the same level of excitement and innovation as more voluntary initiatives, where you are allowed to be more creative and think outside the box.*
Beyond compliance	Moved beyond compliance to create competitive advantage.	*If we speak generally, which I think most people are, about compliance as literally abiding by the law, the answer is absolutely yes, we have moved away. We are moving far beyond compliance, especially if we want this to be a source for competitive advantage.*
From exclusion to opportunities	Screening for ESG factors when looking at investment opportunities instead of exclusion.	*Some private equity firms apply ESG by doing "negative screening" – they will for example have specifically identified sectors that they will not invest in such as the defence sector, tobacco or betting industry. We do not do that but we screen for ESG factors when looking at an interesting investment opportunity and identify areas of improvement where we can come and help them put more effort into ESG issues.*
From exclusion to opportunities	You need to look at risk versus opportunities instead of excluding firms.	*We have moved away from using exclusion criteria and toward seeing opportunities. For example, we bought a company a few years ago. Through Due Diligence, we found an ESG concern. Instead of saying no, we looked* for mitigations*. If we had just been focusing on exclusion criteria, we might not have gone through with the investment. It ended up being a very strong investment for us and our investors, in addition to the local community. In general, you always need to look at risk versus opportunities instead of just saying no.*
Flexibility in application	ESG in portfolio companies is company dependent.	*If you want it (ESG management) to be core to (portfolio) company operations, then it has to be a company where it is part of the core to work with this, where it is part of the DNA, and that is company dependent. We might acquire a company that is already engaged in these questions because it is necessary for them, but there could also be companies that we acquire that had not entered into this without our acquisition.*
Flexibility in application, DNA	Flexible and practical application of ESG.	*In our company, we are not just ticking boxes. We know what ESG stands for, we are flexible and practical about applying it.*
ESG in portfolio companies	ESG is most impactful in portfolio companies.	*If you look at it from an environmental perspective, we do not measure our energy consumption or how much paper we are using per year in. Of course we've had projects (ex. doing black and white printouts per default), but it is more important that we have people in our team that are aware of such ESG concerns in portfolio companies, being significantly bigger and have more employees.*

ESG in portfolio companies, but also to lead by example	ESG is most impactful in portfolio companies, but its also important to lead by example.	*We believe in "leading by example". We recognize that it is through portfolio companies we can make the greatest impact, but it is critical that we lead by example as a firm as well.*
Firm values in recruitment, Shared values	Recruiting people sharing firm values.	*We spend significant time focusing on our values in our recruitment processes. Typically, an investment team member conduct 14 interviews before making an offer. At least half of the time spent in interviews focuses on soft factors, making sure that potential employee's values echo our values. That way you hire people that continues on to "live" the values and the culture that we have, and ESG is an integral part of that.*
Higher engagement	Higher engagement on firm and portfolio company level.	*Working with ESG is creating higher engagement internally, but we are also a lot more engaged with portfolio companies as it provides new interaction points. Traditionally, engagement was mostly about the CEO and the CFO. Now we are engaging with a different set of people within the portfolio companies such as quality managers, environmental managers and communication people, and we see importance of this new engagement in creating good companies.*
Proudness, Talents	Proudness in being a part of something bigger, critical to the younger generation.	*Working with ESG has created a sense of proudness in being part of something bigger than just creating financial value. Especially for the younger talents, this is definitely a critical component.*
Creativity, Smartness	Becoming smarter and more creative working with ESG.	*Working with ESG, we have become smarter and more creative as an investment organization.*
In tune with society	Investors are becoming in tune with stakeholder needs	*By having this agenda (ESG) at the forefront of how we discuss things internally, all investment professionals have become more in tune with society and stakeholder needs.*
Diversity, Shared values	Diverse group of employees, share the same view of ESG.	*We have a diverse group of people in terms of experience and skill set, but one common theme is that they are all concerned with ESG matters in general.*
Diversity	Pushing for diversity in portfolio companies.	*We aim to have diversity on the boards of the companies that we invest in, and if there isn't gender diversity, or just general diversity, we change that.*
Governance.	Governance.	*We want to see our companies paying attention to any kind of governance issue. We have rules for how we govern the boards and how we govern the companies we invest in.*
ESG starts with culture and values	ESG starts with culture and values.	*ESG starts with culture and values, and that has been the building blocks all the way from the beginning.*
Future trends		
Performance measurement	Performance will include more than financial measurements.	*I would think we will be going further in the direction of measuring performance as more than just financial performance.*
Performance measurement	Nordics need to translate efforts into financial impact.	*I may be biased, but I get the sense that sustainability is very closely linked to the Nordic culture, our governance and our social contract. Having said that, we need to become much more systematic and develop measures so that we can prove in quantitative terms how our philosophy is translating into real impact, and not just tell nice qualitative stories.*
Finding future companies	Deal sourcing based on growth following new trends.	*Looking forward, we are talking much more about finding the companies of the future; how do we find those who has structural growth based on different trends?*
Finding future companies, From exclusion to opportunities	Deal sourcing based on value creation.	*I think that we will se that the private equity companies that are creating superior returns have picked their investments differently, that they are investing in companies governed by different principles. Examples being waste reduction or resource efficiency. The type of companies that can benefit are those where the solution is part of the problem so to say.*
Education	Education on how ESG can contribute to each company's strategy and performance.	*A performance culture and a culture promoting ESG is not a contradiction. If you look in the private equity industry, typically performance is measured over a longer period of time, so it is not so much about the next quarter, its rather about what you do during the 4-7 years you own the company. With a longer time frame, you do have time to work with ESG and sustainability issues. The challenge is to*

		make everyone understand how sustainability and ESG can contribute to each specific company's strategy and performance.
Recruitment, Diversity	Need new recruitment processes.	*The business world is becoming more and more complex, and the recruitment strategies that private equity firms have had; is missing out on a lot of competence and insights. How you man your board, and also how you man up the internal organization will need to change. Diversity, both in terms of gender and background is another issue that we need to address better than we are doing now, and even more in the industry.*
Recruitment	Millennials may not be willing to give enough effort to create return.	*To get return is rather hard and systematic work. We need to make sure that we attract talent that are willing to roll up their sleeves and work hard toward getting that return. Recruiting might be a challenge in the future in the sense that the millennium generation would like to work less, and have more flexibility than you might get in the private equity industry.*
People	Younger people are inspired more by building companies than ensuring returns.	*Our purpose is to build strong companies in the Nordic region. A separate part of that, in order to also deliver high returns to our shareholders. My younger colleagues are more attracted to the first part, whereas my older colleagues are more attracted to the second part.*
People	Millennials are more digital, use social media and show more interest in society.	*When I look at the young people entering our industry; they are more born digital, they use social media more, they are more broadly interested in society.*
People	Need people with drive, urgency and a long term perspective.	*The people-element in the ESG agenda is very important. To move at the pace which we need to be moving, we need people with very high drive and a sense of urgency. Private equity is the perfect combination of having a long term perspective and having people who are extremely driven and wanting things to happen now, and not tomorrow.*
People	Skills for the future.	*In the future, the traits you want to see within individuals are the things that always hold true; being smart, driven, humble, curious, having an entrepreneurial spirit and a passion for developing people and companies. I think some of the other things, such as the digital transformation, will come quite naturally.*
People	Skills for the future	*A lot of the turnarounds we are doing are concerning new technology, and the millennium generation is clearly much more naturally educated in those technologies. I think there will be a step up on the technology side.*
People, Creating sustainable future companies	PE is narrow minded. Need to orient toward society and create sustainable companies.	*I think that the private equity industry by nature is a bit narrow-minded. I think it is important that the industry gets more oriented towards the outer society, take part in discussions, and also take the responsibility that it is to create more sustainable companies. And I hope that Millennials will somehow answer that.*
People, Education	ESG is natural to the younger generation.	*I think it is very clear that the younger generation is looking for more than just financial returns. Its very clear to them, that ESG and sustainability is a natural part of what they should do. You need to educate the older, the younger know that it is important.*
People, Working flexibility	New operational roles.	*I think people will move more between having operational roles working within the private equity as investors to get the broader outlook.*
Appetite for change, innovation, Societal purposes	Outlook on the future of the industry.	*In the future, I hope that the private equity industry will be able to marry an appetite for change and innovation with the truly long term perspective, and sometimes the need for patience and persistence. Maybe we'll see an even stronger and more explicit appetite for investing and supporting companies that have a clear societal purpose.*
ESG traction	Finance and PE is gearing up on ESG.	*The financial community and the private equity community especially is gearing up. There is more and more traction within the industry in the area of combining ESG and sustainability with performance.*