KEYNOTE INTERVIEW

The secret to ESG integration? Putting people first

As managers explore optimal ESG integration strategies, Instar's Sarah Borg-Olivier and George So argue the best integration efforts include a tailored, people-centric approach

As ESG has evolved from niche to mainstream over the last decade, the private funds industry deserves some credit for its renewed commitment to delivering on ESG initiatives. As the media and public demand greater accountability around ESG policies, investors increasingly use ESG as a lens through which to understand long-term strategy, management quality and how a company impacts the people and communities it serves. "Stakeholder capitalism" is no longer just a buzzword for the socially conscious go-getters. It's the ethos of businesses and investors looking for sustainable returns in an evolving, volatile economy.

This means ESG can no longer be siloed from the rest of a business. These initiatives must be embedded within a company's business strategy to shape behavior and decision-making, rather than merely appearing in pitch decks. This is no easy task, especially for smaller businesses in the mid-market that don't have the budget for ESG consultants or in-house staff to set the tone. So how does a manager help these businesses flourish in a time of "stakeholder capitalism"?

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Instar is a private equity firm that's made substantial investments in time, capital and talent to implement strong ESG practices at the corporate level and across its portfolio. *Buyouts* sat down with COO and SVP Sarah Borg-Olivier and managing partner George So to discuss their experience developing and integrating the firm's ESG strategy.

Q How does Instar connect its ESG initiatives with the core business of its portfolio companies?

SBO: Our goal at Instar has never been to have a great sustainability strategy. It's to have a business strategy that includes sustainability as a core component. ESG has always been fundamental to how we invest, manage risk and opportunity across our platform and define our corporate purpose, which is to enrich people's lives. With that as our purpose, sustainability is inherently embedded in our strategy. We've found this broadens the aperture of how we look at investment opportunities, how we consider long-term risk and how we approach value creation to generate new revenue opportunities and efficiencies.

Beyond how it shapes our investment plans, we believe people are key to sustainable action and delivering successful business – and ESG – outcomes. These priorities must be ingrained in the leadership team and throughout an organization to engage and empower employees to contribute. In this day and age, it's a competitive differentiator for an employer and can significantly improve talent recruitment and retention.

GS: Our business is all about people, which is why we believe good governance is a key tool in successfully integrating ESG at the corporate level and across the portfolio companies. We partner closely with management teams, engaging industry experts to work alongside them and provide additional support to drive long-term value. While we have the usual cadence of quarterly board meetings, we're not just reviewing financial metrics. We look at each company's progress in all aspects of the business, including ESG performance, and ask what we could be doing differently or better.

We also need to be practical about what small to mid-sized companies can accomplish out of the gate. Our role is to help them build internal capacity and knowledge and to define what's most material for the business. We bring in credible resources and industry experts to help map the strategy and earn our teams' support because there's plenty of evidence that ESG isn't just the right thing to do, it's the right thing to do for the bottom line.

Today, customers, employees and investors are placing more emphasis on ESG matters. We've found the first step in connecting ESG with a company's core business strategy is a governance approach that earns the buy-in of the management team, which means linking sustainability principles to what's material for the business. Looking at safety, if an employee is injured in a preventable situation, they may be entitled to medical or disability-related leave, creating additional costs and the loss of intellectual capital for a business. Employee engagement is another example, looking at how companies can attract and retain talent through ESG initiatives including employee surveys to benchmark the success and opportunities of a company's programs.

Q It's easier to support ESG programs during boom times. Does having an ESG lens help companies better navigate a downturn, even when resources are constrained?

SBO: Sustainability is simply "good business," and the forces driving it are not going away. If ESG sits at the core of your business strategy, the real work of sustainability is continual and likely to make a business more resilient during a downturn. An economic slowdown shouldn't change how a business fundamentally approaches due diligence and risk, and a strong focus on ESG speaks to a management discipline, commitment and focus on other areas of a business that are critical to innovation, long-term performance and value creation.

GS: Downturns can provide management teams with an opportunity to improve and sharpen their company's ESG approach. When the team is working at its full capacity during boom times, it can be difficult to find time to address shortcomings and opportunities to create value for stakeholders. But a downturn can offer some breathing room to improve this aspect of the business and a strong, integrated ESG strategy can help keep employees engaged and fulfilled during periods of challenge and change.

Q What advice would you give other managers who wish to achieve ESG integration?

SBO: In our experience working with portfolio companies, we discuss business goals and competitive differentiators, focusing on what's most material and meaningful for the business, its employees and its stakeholders. We don't simply follow a set of sustainability standards.

Instead, achieving ESG integration is a dialogue and process that takes place over time to set, measure and reflect on a company's goals and the products or solution it delivers to customers or communities. We're looking for progress, not perfection, and it takes a collaborative effort starting with the leadership team setting the tone from the top to drive and build ESG into the business plan for all stakeholder groups.

GS: This means ESG can't be an afterthought. For us, ESG integration is about considering sustainability factors from initial due diligence throughout the full lifecycle of an investment. We take a collaborative approach, working alongside management teams to identify any gaps and opportunities for improvement. ESG is not static but continually evolving and, though sustainability imperatives haven't historically been reported on a balance sheet, almost every ESG metric will ultimately come back to a financial metric.

Again, it's all about people. We look at key material ESG risks and opportunities directly impacting our company, portfolio companies and the communities we serve to protect and create long-term value for all stakeholders. From our diligence process to our focus on involving credible industry experts, including an in-house ESG expert this past year, we've earned the support and commitment from our management teams to make ESG a core component of their business strategies. ■