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Insights

ESG IN M&A TRANSACTIONS - PRESENT AND FUTURE

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The ESG sector has grown at a phenomenal rate over the last 5 years. It has doubled in size over that period and now a quarter of all investible assets globally are being managed with some type of environmental, social or governance mandate.

Practice varies from region to region but the increased prominence of ESG factors in decision-making, risk analysis and valuations globally is significant for M&A professionals and investors.

There are many reasons for this upward trend. Some of this comes from grass roots with consumers significantly changing buying patterns and their investment preferences. Although there are some vocal opponents to ESG being part of investment decisions in the US, in particular, these consumer demands together with targeted shareholder activism has sent a strong signal and given a mandate to those business leaders that wish to take it.

However, there are more fundamental drivers that explain the pace and scale of this change: 30% of businesses globally witnessing operational impacts from climate change. ESG factors are having such a clear impact on the risks and returns of businesses that it is hard to fully understand the value of those businesses without looking at them from an ESG perspective.

Much of the public discussion on ESG factors is driven by large financial institutions and corporates as well as having increased prominence in PE fund raising campaigns and divestitures processes. However ESG factors are not simply a 'luxury item' for large companies and institutions but are also often key to the value of smaller private companies.

It is critical for M&A professionals to understand what this means for them and the companies they advise. In this article, we explain what ESG factors are and what roles they play in M&A transactions.

ESG considerations can be relevant throughout the M&A transaction process, helping to:

i. identify, understand and mitigate risk;

ii. increase target value;

iii. achieve beneficial and long-term synergies for both the buyer and the target; and

iv. reducing friction in the deal and enhancing the likelihood that the deal will close successfully.

As with other diligence topics, a buyer will want to see effective processes to deal with ESG issues. If these processes are not robust then the risk profile may be higher leading to a lower valuation; conversely, if the target can demonstrate good processes and a history of having addressed the risks, then its value can be enhanced.

If a target has strong procedures the deal can often go more smoothly and alignment on ESG issues can help in integration of the target into the buyer, particularly if the buyer is a strategic buyer.

Please read the full article here.

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