

STATE OF PLAY: ESG IN VENTURE CAPITAL

CONTENTS

3 ABOUT THIS REPORT

4 FOREWORD

5 BUILDING VALUE THROUGH BETTER ESG OUTCOMES

6 THE ESG_VC FRAMEWORK

7 OVERALL FINDINGS

11 ACTIONABLE INSIGHTS

13 METHODOLOGY

15 CONTRIBUTORS



ABOUT THIS REPORT

The Australian Investment Council is pleased to publish this inaugural report covering Environmental Social and Governance (ESG) performance in Australian and New Zealand venture capital funds and their portfolio companies.

The report is based on the results of a pilot program that ran in 2023. Ten of the most active venture capital firms across Australia and New Zealand participated in the pilot with 166 portfolio companies contributing data. These portfolio companies are venture-backed businesses from pre-seed to Series C+.

In an industry first in Australia and New Zealand, a common framework – ESG_VC – was used to collect and benchmark data. Managing confidentiality was paramount and to this end, the Council engaged Australian private markets specialist ESG platform Pathzero to manage data collection and warehousing. New Zealand ESG consultancy Sustainability 360 analysed the data, providing the insights contained in this report.

The results of this pilot program will help firms decide their next steps and set clear priorities for this increasingly important issue. It is important to emphasise that this report contains data and insights from a pilot program. Data disclosure was entirely voluntary and therefore not all portfolio companies may have provided all data points. We anticipate this will improve over time as data collection becomes more deeply embedded in businesses.

FOREWORD

The role of investors in non-financial investment performance is increasingly under the microscope, particularly as the links between non-financial and financial outcomes becomes better understood. Internationally, limited partners (LPs) are expecting more detail about ESG management from general partners (GPs). In turn, more GPs are recognising that prudent ESG management can positively impact valuations and that a positive track record can open up opportunities.

A consistent approach to measuring ESG performance can lead to efficiencies in managing a portfolio, setting goals and supporting portfolio companies to build value in their businesses. In 2023, a number of Australian VC firms recognised this and aspired to adopting a single framework to establish a body of industry-level data to support benchmarking. It is an aspiration that the Australian Investment Council is delighted to support.

We are pleased to publish this inaugural report, the result of a successful trans-Tasman pilot program including 10 VC firms and 166 portfolio companies.

ESG is an ever-evolving aspect of investment management, with governments and regulators around the world working on reporting standards and disclosure frameworks. As these instruments are implemented, we know data collection frameworks will also change. Rather than waiting for the dust to settle, a number of Australian and New Zealand VC firms decided to identify a framework and use it as a tool to help drive better performance in their portfolios and to aid responding to growing LP demand for ESG data.

As a new and evolving lens through which to view and manage a portfolio, it is early days and there will always be areas for improvement. It's also important to remember that in VC, portfolio company participants range from early-stage start-ups through to more mature businesses; the earlier stage the business, the earlier on it is likely to be in its ESG journey. Measurement is the first step to management, and we commend the VC firms and portfolio companies that participated in this pilot.

This report is just one way in which the Australian Investment Council supports ESG practices among our members and the private capital industry more broadly. Our ESG Committee comprises specialist practitioners and industry leaders, who are committed to providing forums for learning and information sharing, and developing tools and resources to help firms at various stages of their journey. Our Principles of ESG program provides investment professionals with a baseline understanding of concepts needed to drive outcomes in a portfolio. And we are strong advocates for the industry when it comes to the policy and regulatory settings that will determine how GPs report on ESG.



BUILDING VALUE THROUGH BETTER ESG OUTCOMES

There is growing investor interest in how the assets they own perform across ESG measures. Consumers are increasingly aware of all aspects of the products they buy, employees are driven by values alignment to the companies they work for, and governments are taking a more active role in monitoring the non-financial outcomes of enterprise.

Morgan Stanley research shows 77 per cent of investors pay attention to companies and funds that consider their positive ESG impacts along with their financial returns .

There is also a growing body of evidence of the positive link between good ESG performance and financial performance. For instance, a study by professional services firm Deloitte suggests companies with higher ESG scores also have a higher EV/EBITDA multiple, even after allowing for other business drivers .

With substantial work underway to harmonise international ESG reporting standards, it is essential that the Australian and New Zealand VC industry pays close attention to the ESG performance of their portfolio companies.

Internationally, regulations are being developed to define financially-relevant sustainability information and how this should be disclosed.

In 2023, the International Sustainability Standards Board (ISSB) released a new global baseline for sustainability and climate-related disclosure standards for companies and financial institutions.

In alliance with the ISSB's work, the Australian government anticipates implementing mandatory climate-related financial disclosures and consultation is taking place by the federal Treasury on this . In New Zealand, the government has already enacted the Financial Sector (Climate-related Disclosures and Other Matters) Amendment Act 2021, which mandates climate-related disclosures for certain large entities .

While mandatory ESG reporting may be some way off for local VC firms and their portfolio companies, embedding ESG structures, practices and policies early will make the journey much easier down the line.

However, there continues to be a question about how to do ESG well. With a proliferation of organisations and frameworks across the globe, it can be hard to know the 'right' answer to these questions. Especially in the resource-constrained environment of early-stage companies. This report is designed to assist organisations in working out their next steps on this increasingly important issue.



Dr Marina Lunardi
ESG Manager
Sundrive

"The questionnaire served as a valuable roadmap for our company's sustainability efforts. By meticulously evaluating the questions, we were able to identify key areas requiring focus and establish a prioritised action plan encompassing various aspects of ESG practices. This process not only illuminated areas for immediate improvement but also provided foresight into potential future areas of development.

The versatility of the questionnaire extends beyond the initial assessment. We can leverage the identified focus areas for a multitude of purposes, including applications for government grants, establishing KPIs for ongoing sustainability measurement, and even the creation of internal programs and working teams dedicated to specific sustainability goals. Additionally, the questionnaire proved instrumental in guiding our exploration of potential accreditations or certifications that align with our evolving sustainability strategy."

THE ESG_VC FRAMEWORK




ESG_VC was chosen as the data collection framework for the Australian market.

Developed in the UK, ESG_VC is a venture-ready measurement framework, which asks early-stage companies to answer 53 multiple choice questions spanning 13 ESG objectives.

Designed to provide an entry to ESG scoring, the framework can be easily implemented from Seed to Growth stage, across companies spanning B2B and B2C sectors, resulting in a tangible ESG score and a list of key areas to address to improve ESG performance.

ESG_VC incorporates learnings from other international frameworks such as GRI, SASB and BCorp. It is now used by more than 250 VC firms across the UK, Europe and the US. This provides the opportunity to, in time, benchmark against other VC markets.

Thirteen ESG objectives

 <h3>ENVIRONMENT</h3> <p>Decarbonising and safeguarding our world</p> <ul style="list-style-type: none">• Carbon emissions reduced• Air pollution reduced• Circular economy• Responsible procurement	 <h3>SOCIAL</h3> <p>Building a resilient, engaged and supported workforce</p> <ul style="list-style-type: none">• Staff wellbeing• Parental policy• Measuring diversity• Encouraging diversity and inclusion• Working with community	 <h3>GOVERNANCE</h3> <p>Operating ethically and responsibly</p> <ul style="list-style-type: none">• Data governance and cyber security• Board oversight• Corporate policy• Fair and equal pay
--	---	---

“ESG_VC was founded with a singular focus: to enable early-stage companies to improve their ESG performance.”



Henry Philipson
Co-Founder and
President
ESG_VC

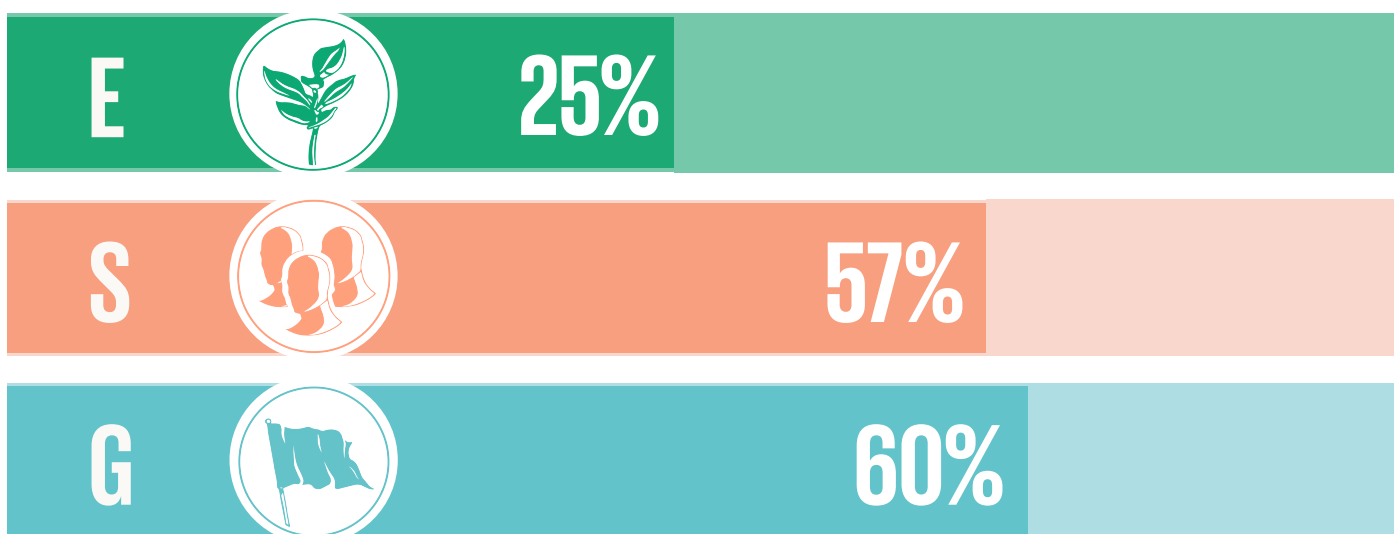
OVERALL FINDINGS

The results from this pilot year provide a baseline from which to set ESG objectives at the fund and portfolio company levels. While there are opportunities to set measurable objectives across E, S and G, clearly environmental measures provide the greatest scope.

We caution readers against comparing outcomes for the three areas - E, S and G - against one another. For example, it is not unreasonable that an early stage technology business may be allocating its scarce resources to cyber security and data privacy, which are governance objectives, rather than carbon emissions.

That said, as start-ups continue on their growth journey, it would be prudent to set environmental objectives in line with investor expectations.

Overall score



A positive relationship between company maturity and ESG scores is observed in the results. It is not surprising to see that mature companies have more established ESG strategies that are integrated into their operational and strategic frameworks than early-stage companies.



"Our industry is on a journey to map and manage the impact of our businesses in a way that works for VC and startups and doing it with our peers has given Airtree greater surety, insight and actionable data. Being able to understand where our portfolio companies sit on ESG, both against the rest of our portfolio and the ANZ VC community more broadly, has been very valuable for us, for our founders and for our LPs."



Harriet Dwyer
Head of Impact
Airtree Ventures

Environment

21%

of companies track and measure their carbon footprint

15%

of companies offset their emissions

5%

of companies have a policy and program in place to achieve net zero carbon



Overall, the results reveal a meaningful opportunity to improve on carbon emissions management in the Australian start-up ecosystem. There's also impetus for portfolio company boards to pay closer attention to ESG considerations, given just 18 per cent have sustainability as a regular agenda item during board meetings.

This is to be expected given the early-stage investing typical of VC and the fact that companies in this dataset were overwhelmingly SaaS products which have a smaller environmental footprint when compared to industries with more physical structures, supply chains and products.

The figures above are overall results and there are variations between sectors, albeit sample sizes for each sector are small. For example, manufacturing performs 23 per cent higher than the average industry score on circular economy. Meanwhile, foodtech and agritech score 21 higher than the industry average on reducing carbon emissions.

Areas with the greatest opportunities to set environmental objectives

Action on climate change was the lowest scoring for ESG outcomes:

Carbon emissions reduced

18%

Air pollution reduced

23%

Responsible procurement and circular economy

29%

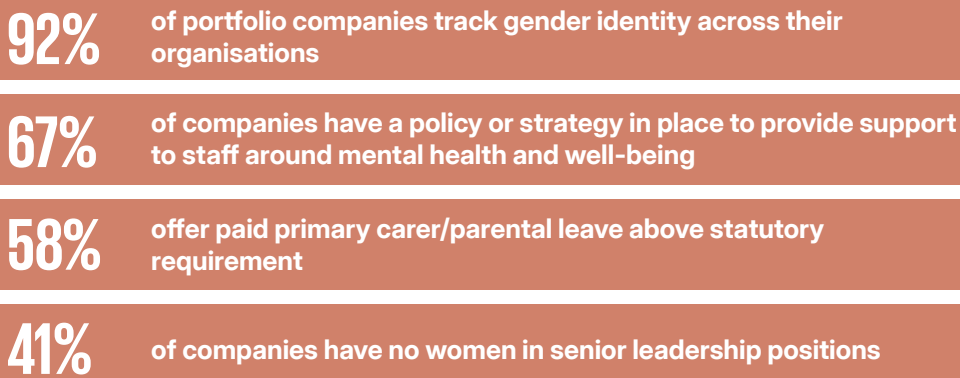


Kate Glazebrook
Head of Impact and Operating Principal,
Blackbird Ventures

This project addresses an industry-wide desire for meaningful data in this space - portfolio companies who want to become more advanced in ESG will be able to compare and track their performance over time and VCs (and their LPs) will have access to portfolio data in the context of ANZ industry benchmarks.

One of the major benefits of this project is that it reduces the workload for portfolio companies, who only need to complete the one survey that they can send to all their participating investors, while providing a greater depth of data across each of the E, S and G metrics. As a working group, we want to move 'ESG' data collection from a box-ticking and risk mitigation exercise to something that creates opportunity.

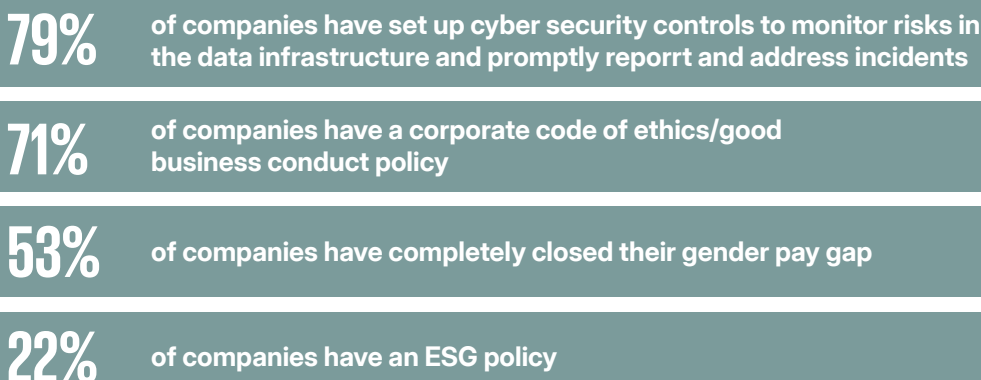
Social



The greatest areas of opportunity are in relation to diversity, equity and inclusion. On gender, 41 per cent of portfolio companies have no women on their boards. When it comes to other groups, 70 per cent of portfolio companies have no board members from underrepresented ethnic backgrounds and 94 per cent have no board members who identify as LGBTQ+.

As with Environment, there are variations across sectors, with education and fintech performing most strongly across Social objectives.

Governance



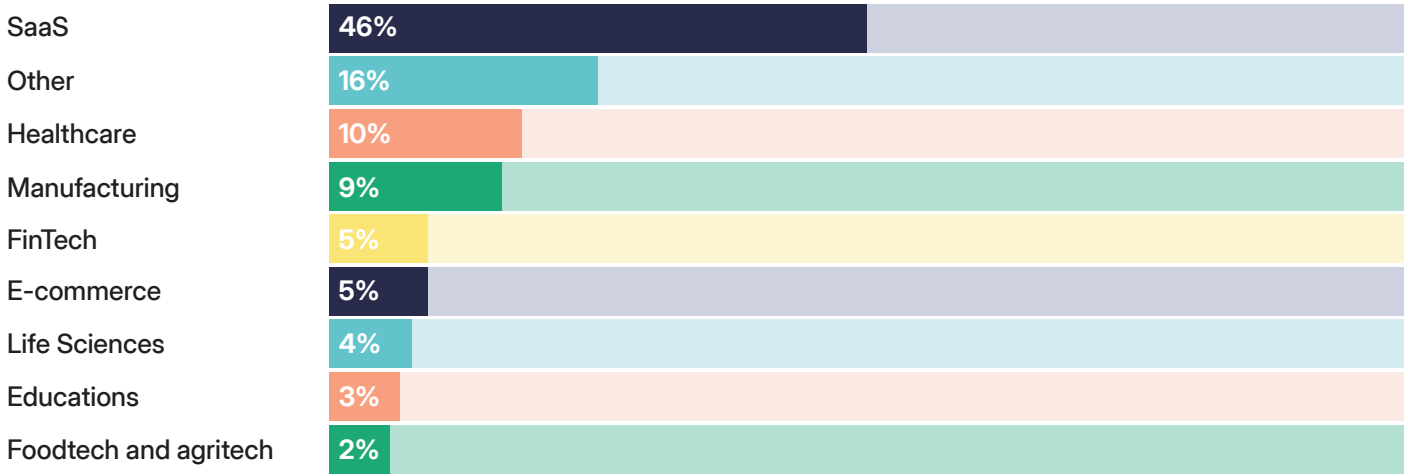
There was little variation on the overall Governance score between sectors.

Within data governance and data security objectives, there are variations in where different sectors place emphasis, particularly in relation to setting up cyber security controls to monitor risks in the data infrastructure and promptly report and/or address incidents.

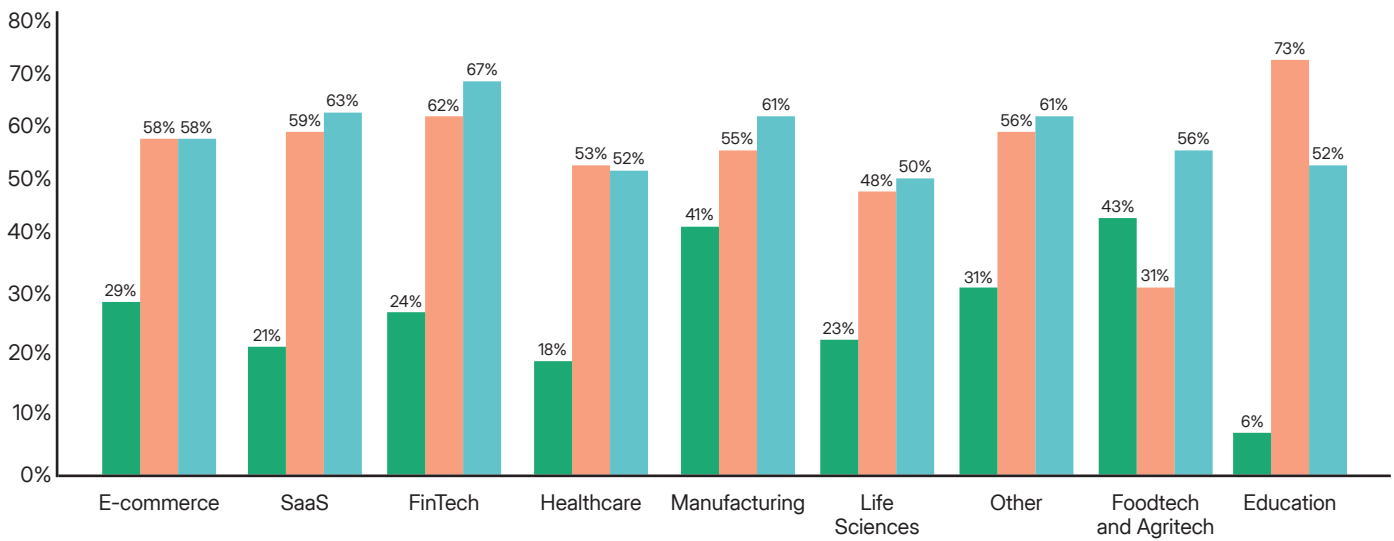
Training on responsible development and use of code / AI systems is a significant opportunity. It is expected portfolio companies would act on this as responsible AI frameworks continue to evolve.

Sector-by-sector results

One hundred and sixty-six portfolio companies across a range of industries and stages of maturity submitted data. Of these, software as a service (SaaS) is by far the largest sector, representing nearly half of the data collected. Many of the other industry groups, including foodtech and agritech, education, and life sciences comprise some very small sample sizes. At this stage of ESG-VC reporting, any comparison between industries should be considered indicative rather than conclusive evidence.



ESG sector by score



As shown in the charts above, the average scores across ESG vary by only eight per cent (40 per cent to 52 per cent). The strongest performance across sectors is on Social metrics, with nearly all industries reporting a score above 50 per cent apart from foodtech and agritech and life sciences.

The overall results for Environment are consistent with the Beringea 2024 ESG_VC measuring companies across the UK and Europe. It is not surprising to see that mature companies have more established ESG strategies that are integrated into their operational and strategic frameworks than early-stage companies.

Portfolio companies

- **Align ESG strategy with core values:** think about the business and its mission, its short-term and long-term strategy, what motivates employees and what matters to customers and investors. This should inform the overall approach to ESG.
- **Identify material ESG issues:** global frameworks like the Sustainability Accounting Standards Board's materiality finder are a good place to start.
- **Get ready to report ESG performance against one or more reporting frameworks:** this will involve implementing robust, digitised data gathering and recording systems, with a view to automating as many of these processes as possible.
- **Ensure effective data management systems in all parts of the business:** this will ensure you are well placed to implement sound ESG data gathering systems across your operations in areas such as energy use and diversity measures.
- **Measure workforce diversity:** this is a key part of making meaningful progress. Portfolio companies are encouraged to develop and implement formal diversity and inclusion strategies. This guide is a good place to start.
- **Monitor and review progress against targets:** the idea is to track the company's progress and, over time review its performance against outcomes that align with the ESG strategy.

Many venture capital portfolio companies starting on their carbon emissions reduction journey will need to begin measuring their carbon footprint to establish a baseline for targeted reductions. This carbon calculator offered by the SME Climate Hub is an example of the range of resources now available that may help portfolio companies understand their carbon emissions and create a plan to reduce them.

By offering guidance, resources and expertise, VC investors have a unique opportunity to encourage and support their portfolio companies to develop and implement stage-appropriate ESG policies and plans.

"OneVentures takes immense pride in contributing to the development of a standardised ESG reporting framework in Australia, a project achieved through the collaborative efforts of 10 Australian venture capital firms and the Australian Investment Council.

By providing participating firms and portcos with the necessary tools, it enables informed, impactful decision-making that aligns with industry standards and sustainability goals. This unified approach to ESG data and metrics will significantly improve data quality and consistency, alleviating the reporting burden for founders. Additionally, it allows portcos to fully comprehend their own environmental, social, and governance scores while creating actionable goals for continuous improvement."



Matt Sinnamon
General Counsel
and COO
OneVentures

VC funds

- **Establish clear expectations for ESG reporting and transparency:** encourage portfolio companies to measure, report and continually improve their ESG performance based on what their peers are doing and feedback from customers and their workforce.
- **Help portfolio companies recognise the ESG issues likely to impact the bottom line:** assess which ESG outcomes are material to mitigate harmful ESG impacts in a more targeted way.
- **Lead by example:** VC investors should demonstrate ESG best practices by having responsible investment policies in place, measuring the fund's ESG performance, setting ESG targets and reporting on them.
- **Foster innovation in areas such as AI ethics and cyber security:** this will help ensure portfolio companies are not only at the forefront of technological advancements but also leaders in responsible and ethical business practices.
- **Advocate for the regular inclusion of ESG issues at portfolio company board meetings:** this will help ensure strategic decisions are made that consider long-term ESG implications.



Navleen Prasad
CEO
Australian
Investment Council

"This report sets an important ESG baseline for the VC industry.

There are great strides being made on many of the key ESG metrics analysed in this report, but there is also clearly more to be done, particularly in the areas of climate and diversity.

We encourage all VC firms to utilise this as a guide for setting priorities and next steps. Use this guide as a checklist, and bring your entire business on board, no matter what stage of growth you are at."

Number of respondents

The analysis in this report is based on data collected from the 10 ESG_VC ANZ working group funds. This comprises ESG_VC datasets from 166 portfolio companies across the group.

Timeframe

The data was collected between June 2023 and September 2023, for the period between 1 July 2022 and 30 June 2023.

Methodology

The working group firms distributed the ESG_VC survey to some or all of their portfolio companies. The companies completed the ESG_VC framework themselves, meaning the dataset is self-reported. The data has not been comprehensively reviewed and remains subjective based on each company's interpretation of the questions asked in the framework.

To aggregate this data into the industry-wide sample used for this report, each company's dataset was anonymised before the fund securely submitted the results to a third party, file-sharing tool, ShareFile. The 166 anonymous datasets were then received by Pathzero who aggregated the results per metric to provide industry results, including overall averages, sector-specific, and stage-specific insights for this report. Caroline Thalund of Sustainability 360 analysed the data and, together with Harriet Dwyer of Airtree, produced the detailed report for working group members.

Voluntary disclosure

It is important to emphasise that this report contains data and insights from a pilot program. Data disclosure was entirely voluntary and therefore not all portfolio companies may have provided all data points.

Confidentiality

Managing confidentiality was paramount and to this end, the Council engaged Australian private markets specialist ESG platform Pathzero to manage data collection and warehousing.

Acknowledgements

The Australian Investment Council would like to thank all the firms and funds that participated in the pilot.

We also thank the following contributors to the project:

Alexandra Cain

Harriet Dwyer, AirTree

Carl Prins, Pathzero

Victoria Pymm, Australian Investment Council

Caroline Thalund, Sustainability 360

Robyn Tolhurst, Australian Investment Council

We extend a special thank you to Henry Philipson at Beringea for the generosity of his support throughout this project.

CONTRIBUTORS

Research partners

"Pathzero is thrilled to have contributed to this first-of-its-kind report examining ESG practices within the VC sector.

The insights will help us better understand the ESG landscape in portfolio companies, including both strengths and areas for improvement, especially related to emissions measurement where we now know there is a critical gap between reporting and plans for reduction.

It's an exciting opportunity for the VC sector to consider how it can best drive positive changes, and we're eager to see the impact these insights could have on ESG reporting and metrics within portfolios. "



Carl Prins
CEO
Pathzero



ESG Data Partner



Caroline Thalund
CEO and Founder
Sustainability 360

"Over the last year, I have had the pleasure of being a part of the journey that the ANZ VC industry is on, with support from the Australian Investment Council. It has been fantastic seeing so many VCs join forces to collectively work towards measuring ESG performance, standardising the collection process, and paving the way for greater impact.

This pilot project resulted in a large volume of data from 166 companies across 56 metrics. Conducting the research, analysing the data and writing this report allowed me to extract rich and valuable insights that I hope will be valuable to the VC industry in Australia and New Zealand."



Pilot participants

airtree

Alberts

BLACKBIRD

BRANDON
CAPITAL

B BREAKTHROUGH
VICTORIA

GiantLeap

**MAIN
SEQUENCE**

mandalay vc

1/ ONE
VENTURES

Square Peg 

Level 12, Aurora Place
88 Phillip Street
Sydney, NSW 2000
T: +61 2 8243 7000
investmentcouncil.com.au



The Australian Investment Council is the peak body representing Australia's private capital industry, comprising over 200 leading domestic and international private capital firms operating in Australia. Our members comprise private equity, venture capital and private credit funds, as well as institutional investors and leading corporate advisors. Our members form part of a dynamic industry that supports entrepreneurship, commercialises research and empowers established businesses to grow and evolve. Our industry employs approximately half a million Australians and contributes roughly three per cent to Australia's GDP. The Australian Investment Council empowers private capital to invest in Australian businesses, ideas and communities.