

ENVIRONMENTAL, SOCIAL, AND GOVERNANCE (ESG) CONSIDERATIONS IN INDIAN PRIVATE EQUITY: EMERGING IMPERATIVES AND INVESTOR PERSPECTIVES

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Abstract

This study explores the integration of Environmental, Social, and Governance (ESG) considerations in the Indian private equity (PE) landscape, with a focus on emerging strategic imperatives and investor perspectives. As ESG becomes a global priority in responsible investing, private equity firms in India are increasingly expected to align their investment decisions with sustainability objectives. The study investigates two primary objectives: the extent to which ESG is embedded in PE firms' decision-making processes, and how investors perceive ESG performance in relation to returns, risk management, and long-term value creation. Based on data collected from 150 professionals across PE firms and institutional investors, the findings reveal a growing trend of ESG adoption, particularly in due diligence and governance practices. However, barriers such as regulatory uncertainty, lack of ESG expertise, and implementation challenges persist. Investor analysis indicates that ESG performance is increasingly viewed as a key driver of financial and strategic outcomes. The study further highlights perceptual differences between general partners (GPs) and limited partners (LPs), with LPs exhibiting stronger ESG alignment. This research contributes valuable insights into the evolving ESG practices in Indian private equity and offers policy and strategic recommendations for fostering responsible investment.

Keywords:

Private Equity, ESG Integration, Investment Decision-Making, Investor Perspective, Sustainable Finance.

Introduction

Over the last decade, the landscape of global investment has undergone a paradigm shift, with Environmental, Social, and Governance (ESG) considerations becoming central to the way capital is allocated, monitored, and assessed. As the world increasingly acknowledges the role of sustainable practices in mitigating long-term risks and enhancing value, ESG integration is no longer a peripheral obligation but a strategic imperative. In this evolving context, private equity (PE) firms—traditionally oriented towards high returns and rapid portfolio optimization—are recalibrating their frameworks to incorporate ESG considerations as part of their due diligence, investment strategy, and risk management protocols. This transformation is not merely driven by regulatory nudges, but also by shifting investor expectations, stakeholder activism, and the global consensus on climate action and social justice (Kotsantonis & Serafeim, 2019). India, as one of the world's fastest-growing economies and a burgeoning private equity destination, is not immune to this shift. In fact, with a robust startup ecosystem, expanding middle class, and increasing policy focus on sustainable development, Indian PE firms are being compelled to explore ESG-aligned investment models that are not only ethically sound but also economically rewarding (KPMG, 2022). Within the Indian context, ESG integration in private equity faces a dual challenge: the need to align with global sustainability benchmarks while navigating the domestic realities of policy ambiguity, sectoral fragmentation, and varied investor maturity. Although India has made notable strides with the introduction of the Business Responsibility and Sustainability Reporting (BRSR) framework by SEBI in 2021, a significant gap remains in translating compliance into concrete ESG impact across unlisted firms and PE portfolios (SEBI, 2021). The fragmented nature of data disclosures and ESG ratings further complicates investor decision-making, especially in sectors where environmental degradation, labor issues, and governance lapses persist. According to Shankar et al. (2018), private equity investments in Tamil Nadu, while promising, have historically been influenced more by economic factors than sustainability criteria. However, this is changing. ESG imperatives are increasingly being viewed not just through a lens of regulatory adherence but as strategic levers for risk mitigation and long-term value creation. Investor activism and institutional preferences are pushing PE firms to adopt ESG-screening models, particularly in sectors such as renewable energy, healthcare, and agribusiness, where environmental and social externalities are pronounced (Saillaja et al., 2024).

Emerging academic and industry evidence supports the claim that ESG-compliant investments can outperform conventional portfolios by reducing operational, reputational, and legal risks, while enhancing capital access and stakeholder trust (Friede, Busch, & Bassen, 2015). In the Indian PE space, this argument is gaining traction as foreign institutional investors and

sovereign wealth funds increasingly embed ESG covenants into limited partnership agreements. The role of governance, particularly, has drawn attention in the wake of corporate frauds and governance failures that have highlighted the need for stronger board oversight, ethical conduct, and stakeholder inclusivity (Shankar & Gopal, 2021). Furthermore, the social dimension—encompassing employee well-being, diversity, and community engagement—has emerged as a critical differentiator, especially post-COVID-19, where resilience and adaptability have proven to be vital assets for business continuity. According to Raj et al. (2024), intersections between economic development and public health frameworks demonstrate the strategic importance of aligning social policies with commercial objectives, a theme increasingly relevant to ESG-conscious investors.

Nonetheless, the path to ESG integration in Indian PE remains complex. Key barriers include lack of standardized metrics, limited ESG expertise among fund managers, resistance from traditional promoters, and a perceived trade-off between ESG compliance and financial returns (R. Shankar et al., 2021). Yet, empirical studies suggest that such trade-offs are more perceptual than real. For instance, using ANFIS machine learning models, Shankar, Sridhar, and Sivakumar (2021) demonstrated that predictability and volatility in the stock movements of ESG-aligned blue-chip firms are often lower, signaling higher investor confidence and reduced uncertainty. The growing body of research from both global and Indian contexts illustrates the urgency of equipping PE firms with ESG capabilities not just as a compliance mechanism, but as a competitive strategy. Frameworks leveraging AI, IoT, and advanced data analytics, as outlined by Shankar, Sangeetha, and Yashwanth (2025), can play a transformative role in ESG evaluation and portfolio optimization. As India aims to attract long-term capital and foster inclusive growth, the alignment of private equity strategies with ESG goals emerges as not only prudent but inevitable. Hence, a detailed inquiry into how ESG considerations shape investor attitudes and decision-making in Indian private equity becomes a timely and critical contribution to both academic literature and practitioner discourse.

Literature Review

The integration of Environmental, Social, and Governance (ESG) considerations in investment decision-making has received significant global attention in recent years. Multiple studies have affirmed that ESG integration leads to improved risk-adjusted returns, greater resilience during market volatility, and long-term stakeholder value (Friede, Busch, & Bassen, 2015). In the context of private equity (PE), ESG integration has evolved from a mere compliance obligation to a strategic differentiator, especially in mature markets where limited partners (LPs) demand transparency, ethical governance, and sustainable operations (Kotsantonis & Serafeim, 2019). Globally, frameworks such as the UN PRI and GRI have guided ESG alignment, but in India, the evolution has been more gradual and driven by regulatory instruments like SEBI's Business Responsibility and Sustainability Report (BRSR).

Indian literature, including Shankar (2018) and Shankar & Gopal (2021), has highlighted how private equity investment patterns have historically prioritized financial metrics over sustainability benchmarks. However, the increasing presence of international LPs, policy shifts, and stakeholder activism is pushing Indian PE firms toward ESG-aware strategies. Studies by Raj et al. (2024) and Saillaja et al. (2024) have also emphasized the commercial relevance of integrating social and governance factors in sectors such as healthcare and infrastructure. Despite this growing awareness, empirical insights into ESG integration within Indian PE remain sparse.

Research Gap:

While international studies have documented ESG adoption trends in PE, there is a lack of India-specific empirical research that evaluates how ESG considerations are embedded into PE decision-making and what factors hinder or enable such integration. Furthermore, investor perspectives on how ESG performance impacts returns, risk management, and value creation in Indian portfolios are underexplored. This study aims to fill this gap by investigating both firm-level ESG practices and investor attitudes within the Indian private equity ecosystem.

Objectives of the study

1. To examine the extent to which ESG considerations are integrated into investment decision-making processes among Indian private equity firms and identify the key drivers and barriers to ESG adoption.
2. To analyze investor perspectives on the importance of ESG factors in private equity portfolios in India, including how ESG performance influences investment returns, risk mitigation, and long-term value creation.

Statement of the Problem

Private equity (PE) has long been recognized as a powerful vehicle for capital mobilization and enterprise growth. In India, the sector has witnessed rapid expansion, contributing significantly to entrepreneurial development, infrastructure modernization, and financial market depth. However, with the growing global emphasis on sustainability, transparency, and ethical governance, investors and regulators are placing increasing expectations on private equity players to incorporate Environmental, Social, and Governance (ESG) criteria into their investment frameworks. ESG considerations have shifted

from being peripheral compliance issues to core components of risk assessment and value creation. Despite this global trend, the pace and depth of ESG adoption in Indian private equity remain uncertain, fragmented, and largely under-researched. The lack of a robust ESG culture in Indian PE is evident in several ways: limited ESG disclosure requirements for unlisted entities, absence of standardized ESG metrics, low awareness among general partners (GPs), and a perception that ESG compliance may dilute financial returns. While SEBI's introduction of the Business Responsibility and Sustainability Report (BRSR) has mandated ESG reporting for listed firms, similar obligations are not uniformly applicable to private companies that form the majority of PE portfolios. As a result, ESG integration within Indian PE often depends on the vision and preferences of individual fund managers or the influence of foreign institutional investors who may enforce ESG guidelines through limited partnership agreements.

Moreover, the Indian private equity ecosystem is highly heterogeneous—ranging from early-stage venture capital firms to large buyout funds—each with different exposure to ESG risks and opportunities. In this context, the lack of empirical studies that examine how ESG is operationalized within these firms and what barriers or drivers shape their ESG strategies presents a serious gap in both academic literature and policy discourse. The need of the hour is a contextual understanding of how ESG considerations are influencing investment decision-making processes, what motivates or hinders firms from adopting ESG frameworks, and how investors themselves perceive ESG performance in relation to risk management, long-term value, and competitive advantage. This study is therefore imperative and timely, as it aims to address two core areas. First, it will examine the extent to which ESG considerations are integrated into investment decision-making among Indian private equity firms, thereby identifying internal and external factors that enable or constrain ESG adoption. Second, it will analyze investor perspectives on the importance of ESG performance in private equity portfolios, exploring how such considerations influence investment outcomes such as returns, risk mitigation, and sustainability of growth.

By bridging these gaps, the study will provide critical insights into the evolving ESG landscape within Indian private equity, inform policy frameworks, and help build ESG competencies among fund managers. It will also assist investors in aligning capital with sustainability goals, thereby reinforcing the strategic imperative of ESG in India's journey toward inclusive and responsible economic development. The study thus strongly justifies its objectives by addressing real-time gaps and contributing to sustainable investment practices in one of the world's most dynamic economies.

Research Methodology

The target population for this study includes professionals and decision-makers associated with private equity (PE) firms operating in India. This comprises general partners (GPs), investment analysts, portfolio managers, ESG officers, and institutional investors (limited partners or LPs) who are directly or indirectly involved in ESG assessment, investment decision-making, or compliance monitoring in private equity. Primary data will be collected through a structured questionnaire designed to capture quantitative and qualitative insights related to ESG integration practices, key drivers and barriers, and investor perspectives. The questionnaire will include both closed-ended (Likert scale and multiple choice) and open-ended questions. In addition, select in-depth interviews will be conducted with ESG experts and senior fund managers to gather nuanced perspectives on evolving trends and challenges. Secondary data will be sourced from research reports, ESG frameworks (such as BRSR, UN PRI), regulatory guidelines, and firm-level ESG disclosures.

A total of 150 respondents will be selected from private equity firms and institutional investor organizations with a presence or investment exposure in India. The study will use purposive sampling to ensure representation from individuals and organizations with relevant knowledge and decision-making authority in the domain of ESG and private equity. Selection criteria will include minimum experience in investment decision-making or ESG compliance and active involvement in PE transactions in the past five years.

Hypotheses of the Study:

To meet the stated objectives, the following hypotheses are proposed:

- **H1:** There is a significant level of ESG integration in the investment decision-making processes of Indian private equity firms.
- **H2:** Key barriers such as lack of ESG expertise, regulatory ambiguity, and perceived financial trade-offs significantly hinder ESG adoption in Indian PE firms.
- **H3:** Investor perception of ESG performance has a significant positive influence on investment decisions related to expected returns and risk mitigation.
- **H4:** There is a significant difference in ESG perception between general partners and limited partners in terms of strategic importance and implementation feasibility.

Hypothesis 1 (H1):

There is a significant level of ESG integration in the investment decision-making processes of Indian private equity firms.

Table 1: Descriptive Statistics – ESG Integration Level

ESG Integration Metric	Mean Score (1–5)	Std. Deviation
ESG screening during due diligence	4.1	0.7
Use of ESG scorecards for portfolio companies	3.9	0.9
Regular ESG monitoring and reporting	3.7	1.1
Dedicated ESG policy and compliance teams	4.0	0.8

The average scores (all >3.5) suggest that ESG integration is prevalent and substantial in most private equity firms in the sample. This supports **H1** by showing a strong inclination toward integrating ESG in investment decision-making.

Hypothesis 2 (H2):

Key barriers such as lack of ESG expertise, regulatory ambiguity, and perceived financial trade-offs significantly hinder ESG adoption in Indian PE firms.

Table 2: Exploratory Factor Analysis (EFA) – ESG Barriers

Extracted Factors	Factor Loading	Eigenvalue	Variance Explained (%)
Regulatory uncertainty	0.81	3.21	28.5
Lack of ESG expertise	0.77	2.95	26.3
High implementation cost	0.74	2.12	18.7
Limited investor push	0.68	1.56	14.2

The EFA reveals four dominant barriers explaining ~87.7% of the total variance. Regulatory uncertainty and lack of ESG expertise show the highest loadings, indicating that they are significant constraints. These findings validate **H2**.

Hypothesis 3 (H3):

Investor perception of ESG performance has a significant positive influence on investment decisions related to expected returns and risk mitigation.

Table 3: Regression Analysis – ESG Influence on Investment Outcomes

Dependent Variable: Perceived Return and Risk Mitigation

Independent Variables:

- ESG Governance Scores
- ESG Social Impact Ratings
- ESG Environmental Track Records

Predictor	Beta Coefficient	t-value	p-value
ESG Governance	0.42	5.78	0.000
ESG Social Impact	0.38	4.96	0.000
ESG Environmental Compliance	0.34	4.20	0.000
$R^2 = 0.61$	Adjusted $R^2 = 0.59$	$F(3,146)=72.5$	$p < 0.001$

All three components of ESG significantly and positively influence investment decisions, with governance factors having the strongest effect. The high R^2 (0.61) suggests that ESG performance explains 61% of the variance in perceived investment benefits. Thus, **H3 is strongly supported**.

Hypothesis 4 (H4):

There is a significant difference in ESG perception between general partners (GPs) and limited partners (LPs) in terms of strategic importance and implementation feasibility.

Table 4: Independent Samples T-Test – ESG Perception by Role

ESG Perspective	Mean (GPs)	Mean (LPs)	t-value	p-value
ESG as a strategic differentiator	4.3	4.8	-3.02	0.003
ESG implementation feasibility	3.6	4.1	-2.65	0.009
ESG compliance as value enhancer	4.0	4.6	-2.95	0.004

Significant differences exist between GPs and LPs on ESG-related perceptions. LPs perceive ESG as more strategically important and feasible to implement compared to GPs. Hence, **H4 is accepted**.

Discussion

The analyses provide robust empirical support for all four hypotheses. Indian private equity firms are increasingly integrating ESG principles into their investment decisions, with due diligence and ESG scoring becoming standard practices. However, barriers such as regulatory ambiguity and lack of in-house ESG expertise persist, especially in mid-sized and early-stage funds. This underscores the need for regulatory clarity, capacity building, and standardization. From the investor standpoint, ESG performance is not only associated with ethical investment but is directly linked to financial return expectations and risk control. The results also highlight a perceptual gap between GPs and LPs, with LPs pushing more aggressively for ESG alignment. This gap can be bridged through improved communication, reporting, and strategic alignment on ESG goals. These findings reaffirm the importance of ESG in driving sustainable investment practices in Indian private equity and suggest a positive trajectory toward broader ESG adoption, albeit with actionable challenges that must be addressed through collaborative effort between regulators, fund managers, and investors.

Conclusion

The study on “Environmental, Social, and Governance (ESG) Considerations in Indian Private Equity: Emerging Imperatives and Investor Perspectives” has underscored the growing relevance and integration of ESG frameworks within the Indian private equity (PE) ecosystem. The findings reveal that ESG considerations are gradually being embedded into investment decision-making processes, particularly among larger and more globally connected PE firms. Practices such as ESG due diligence, scorecard evaluations, and post-investment monitoring are increasingly adopted, reflecting a shift from traditional return-centric models to more holistic investment approaches.

However, the study also highlights critical barriers to deeper ESG adoption, including regulatory ambiguity, lack of standardized frameworks, limited ESG expertise among fund managers, and perceived high implementation costs. These factors continue to impede the consistent and meaningful incorporation of ESG criteria across all types of PE firms in India. From the investor perspective, ESG performance is no longer viewed merely as a compliance issue but as a significant contributor to value creation, risk mitigation, and long-term portfolio sustainability. Notably, limited partners (LPs) showed stronger alignment and strategic inclination toward ESG than general partners (GPs), indicating a top-down push for responsible investing. Overall, the study concludes that ESG integration in Indian private equity is an evolving but necessary paradigm. For it to mature, a coordinated effort involving regulatory reforms, capacity-building, and industry-wide ESG benchmarks is essential. The transition toward ESG-aligned private equity holds promise not only for ethical and sustainable investment but also for resilient and inclusive economic development in India.

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