ESG Forecast: Trends for 2025

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Introduction

In 2024, Malk's network of private market investors and corporate clients continued to position management of environmental, social, and governance areas as a core strategic priority. Amidst a maturing ESG landscape, shifting regulatory and political priorities, and a continued focus on value creation and returning capital, Malk observes a through-cycle mentality for private market leaders. GPs that have invested in developing mature ESG functions are well-poised to prioritize material issues and navigate market headwinds. Malk continues to see an expansion in ESG functional responsibilities from risk mitigation to value creation and strategic planning, emerging compliance responsibilities, and a strategic reprioritization of issues as investors prepare for 2025.

Key ESG Trends for 2025

1. **Transition from ESG growth era to ESG maturity era.**

   As management of ESG-related investment risks and value-drivers matures among private market and alternatives investors, ESG functions across GPs are aligning on a core set of 'best practice' programming. Based on increased LP and GP experience integrating ESG investment controls, Malk observes consolidation of the most value-additive practices throughout fund management, investment diligence, and portfolio engagement. Further, as independent ESG functions mature and investment team awareness increases, ESG is being managed better but is moving out of the spotlight as an emerging topic. Simply put, ESG functions are transitioning from a focus on innovation to effective implementation.

   Private market GPs are increasingly managing ESG well across assets as a core fiduciary responsibility, rather than an emerging differentiator for fundraising and investor relations. The growth era of sustainability and ESG innovation in private markets has transitioned to an era of consolidation marked by better data standardization, more mature portfolio engagement, and increased portfolio literacy. As GPs recalculate ESG goals, many are transitioning from using ESG as a lever for fundraising and external engagement to prioritizing internal management of material investment risks and opportunities. Malk anticipates a continued shift towards firms more quietly managing discrete ESG areas well across portfolio assets, instead of as a macro issue for fund differentiation.

2. **Tradeoffs in prioritization of ESG issues under shifting political and market factors.**

As market demand, regulatory priorities, and geopolitical concerns shift, Malk has observed a strategic reprioritization of environmental, social, and governance issues for LPs and GPs. While many ESG issues (e.g., worker health and safety, environmental management, product safety) are considered based on materiality, some key ESG issues have been prioritized across sectors in response to emerging risks.

First, climate is increasingly seen as a baseline issue for GPs and corporates. Management of climate change transition (i.e., decarbonization and energy transition) and physical (i.e., acute or chronic weather events) risks is expanding from a material factor dependent on asset exposure to a fundamental tenet of portfolio and asset management. Once a priority for high-emitting companies and funds with significant exposure, portfolio assets across sectors increasingly face greenhouse gas (GHG) emissions and climate risk disclosure requirements as stakeholders map value chain emissions and prepare for climate risk planning. Regulatory disclosure requirements (e.g., CCDAA, CSSB, CSRD, SECR) mandating emissions and climate risk disclosures across jurisdictions have been a key driver of demand, which Malk anticipates may face legal challenges but are unlikely to be disrupted as a growing trend.

Second, diversity, equity, and inclusion (DEI) has been increasingly deprioritized in response to successful campaigns to roll back affirmative action and wavering appetite for DEI programming. Once a focal point of investor interest, corporates have faced litigation and regulatory scrutiny in response to affirmative action targets, hiring and promotion quotas, and recruitment criteria. Successful regulatory campaigns to challenge the legality of affirmative action in the U.S. have been a primary driver, which appears likely to continue under the second Trump Administration. Malk anticipates resiliency in many internal facets of DEI programming, including anti-discrimination and harassment controls, internal employee resources, and diverse training programs, but projects a decrease in external DEI commitments and disclosures.

Third, shifting geopolitical conflicts have increased focus on trade compliance, supply chain resiliency, and human capital in affected regions as governance and social issues. Heightened sanctions and export controls have prompted investors to prioritize mature trade compliance controls, including sanctions and restricted parties screening, particularly for advanced technology and military applications. Trade restrictions and anticipated tariffs have prompted a broader reconfiguration of supply chains, including increased nearshoring of critical vendors, leading to an enhanced focus on the resiliency of and sustainability of supply chains. Finally, talent pools in conflict geographies (e.g., Israel) have been disrupted, impacting investors with exposure to key sectors (e.g., software) in the country.

3. A rise in ESG and sustainability regulatory compliance.

While voluntary reporting cycles for investor (e.g., PRI) and corporate (e.g., CDP, SBTi) disclosure frameworks have been managed by ESG functions to date, GPs and their portfolio assets must prepare for the onset of an era of ESG compliance. 2025 marks the initial reporting cycle for key regulations; the E.U.'s Corporate Sustainability Reporting Directive (CSRD) and California's Climate Corporate Data Accountability Act (CCDAA) initiate reporting for large companies in Q1 2026 for fiscal year 2025 data. In addition, the E.U. Carbon Border Adjustment Mechanism (CBAM) final transition year is 2025, mandating companies to finalize calculations on the carbon-intensity of imported goods to prepare for declarations in 2026.

As such, Malk anticipates that GPs will be required to increasingly dedicate resources to preparation for ESG regulatory compliance across covered portfolio assets. Corporates that meet in-scope reporting criteria for business operations in either jurisdiction, must prepare disclosures and ensure sufficient ESG data (e.g., Scope 1 & 2 emissions) and disclosures (e.g., climate-related financial risk analysis) are maintained. Each regulation presents unique challenges; in the U.S., many companies have lacked sufficient climate risk analysis to prepare for California climate disclosure regulations, and in the E.U. reporting entities must prepare for extensive disclosures under the CSRD to ensure compliance. Further, companies with in-scope operations in Europe must navigate additional emerging E.U. regulations (e.g., CSDDD) as well as new and/or stricter jurisdictional regulations (e.g., Norway Transparency Act) across jurisdictions.

4. **Continued improvements in ESG data quality and increased focus on linking data with value creation.**

   As ESG functions mature across private market GPs, ESG data has increasingly been standardized and has improved in quality and availability. Malk has observed a general trend in the improvement of portfolio environmental (e.g., energy utilities, GHG emissions, resource consumption), social (e.g., safety incidents, employee turnover, workforce representation), and governance (e.g., cybersecurity breaches, noncompliance incidents) data availability year-over-year. While investors have stress-tested different performance metrics throughout the ESG growth period and firms maintain individualized KPIs where right-sizing metrics make sense, GPs in the U.S. are largely focusing on a set of standard ESG KPIs aligned with the ESG Data Convergence Initiative (EDCI).

   High-quality ESG data generally requires two to three years of collection to establish. Malk typically notes poor data quality in initial KPI collection cycles, particularly for growth-stage and middle-market companies. In turn, data quality and availability improve in subsequent years as GPs support portfolio companies with enhanced resources (e.g., consultants, software, centralized corporate functions) for data collection and validation. While corporates frequently still lack sufficient centralized capacity to manage ESG data, Malk projects that many private market funds in the U.S. are approaching portfolio ESG data maturity in 2025 collection cycles, supporting enhanced analysis of opportunities to bolster returns. In Europe, Malk has observed that ESG data in private market portfolios has already reached maturity, with GPs already transitioning their focus to value creation planning.

   Standardized and high-quality ESG metrics which can be benchmarked year-over-year present an opportunity for GPs and portfolio companies to link ESG performance with financial performance. Malk anticipates a continued effort to identify how ESG performance impacts top-line revenue growth and bottom-line operational costs to support value-creation planning throughout hold periods. Trends in ESG performance linked with investment returns can demonstrate mature functional capacity and profitability in exit planning, a continued area of focus for GPs in 2025.

5. **A push towards returning capital across private markets; Using ESG as a lever for exit planning.**

   Malk's GP client base continues to face pressure regarding portfolio performance and capital returns to LPs. As investors anticipate favorable regulatory tailwinds for dealmaking and face investor demand for exits, Malk anticipates that GPs will increasingly integrate ESG operations and data in exit planning. Strong ESG performance and mature ESG-aligned corporate functions (e.g., human capital, compliance, procurement, EHS, information security, quality management) present operational areas for value creation that support profitability and may enhance exit multiples, alongside other core business activities.

   ESG strategic planning initiatives typically include coaching management teams on aligning ESG integration with financial performance and commercial interests. Sample activities may include analyzing ESG performance data to identify cost-cutting (e.g., reduced attrition/incident rates) or revenue-generative (e.g., increased ESG-linked contract terms). GPs may also engage third-party agencies for certifications or vendors for audits (e.g., cybersecurity, EHS) to validate strong ESG performance to demonstrate to prospective buyers that assets present 'turnkey' ESG capacity, reducing operating costs for investors to stand up ESG operations across corporate functions. As investors increasingly prioritize returning capital, Malk anticipates increased integration of ESG into exit planning and linkages to financial performance in 2025.

6. **Using ESG pushback as a lever to strategically reprioritize commitments and corporate action.**

Finally, Malk anticipates that continued pushback on ESG issues from conservative LPs, the Trump Administration, and activist investors will present an opportunity for corporates and GPs to reprioritize commitments and strategic planning. In 2024, major public U.S. companies (e.g., Target, Tractor Supply, Walmart, John Deere) and investment firms (e.g., BlackRock) experienced anti-ESG activist scrutiny and litigation, particularly for corporate DEI programming. The rise of anti-ESG litigation, and scrutiny of affirmative action, has commonly been seen as a leading indicator of headwinds for ESG integration. However, Malk believes that macro-level ESG pushback also presents an opportunity for corporates to right-size their focus to prioritize more material ESG issues. For example, following anti-ESG stakeholder backlash, Tractor Supply has re-prioritized land conservation and biodiversity protections over their prior DEI and emissions reduction commitments.

As private market corporates and investors prepare for similar scrutiny, Malk believes that executive teams can use pressure to strategically reprioritize ESG issues most material for operations and linked to strong financial returns. For example, instead of adopting generic ESG targets and programming aligned with peers and trending issues, Malk projects that corporates and investors facing anti-ESG scrutiny will increasingly focus on common-sense ESG issues material for their operations. Prioritization of strong worker health and safety performance, cybersecurity risk management, environmental compliance, and employee engagement and retention, for example, present ESG performance areas that can be directly linked to operational cost reductions and present decreased risk of litigation and reputational scrutiny.

Malk anticipates that a re-prioritization of ESG issues based on the materiality of business impacts will be a part of a broader transition from management of ESG as a single topic to increased focus on ESG issue areas as distinct corporate functions. Responsible corporate management of environmental, social, and governance-related risks and opportunities present a decreased risk of anti-ESG activist scrutiny, relative to broader programmatic ESG commitments. As private markets continue to evolve in 2025, Malk anticipates that GPs and LPs may increasingly refine materiality thresholds and focus on common-sense ESG programming in a more sensitive political environment.

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About Malk Partners

Malk Partners is the preeminent advisor to private market investors for creating and protecting value through environmental, social, and governance ("ESG") management and impact investing. Founded in 2009, Malk Partners advises many of the world's leading alternatives managers investing across private equity, growth equity, venture capital, and private credit by helping them define ESG goals, achieve ESG results, and guide their portfolio companies in driving value creation and mitigating risks. The firm is headquartered in New York. For more information about Malk Partners, please visit www.malk.com.