Materiality Matters: How startups and VCs need to approach ESG

ESG principles have gained significant traction in recent years, but the conversation surrounding them continues to be clouded in misunderstanding. The prevailing notion that “starting with anything that looks like sustainability” will suffice has led startups and investors astray.

Temps de lecture : minute

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The key to doing ESG right is in one word: materiality. What ESG factors are actually financially relevant and impactful for a given company? For venture capitalist (VC) investors and the startups they invest in, materiality is the foundation for using ESG as a tool for investing and scaling more meaningfully and responsibly, rather than just treating it as a compliance, tick-box exercise.

What is Materiality and why does it matter?

Materiality refers to the process of identifying and focusing on ESG issues that have the greatest financial impact on a specific business. This contrasts sharply with the more superficial approach of ticking off generic sustainability checklists, often incentivised by ESG reporting or the desire and pressure to publicly demonstrate one’s superficial ESG credentials.

For startups, adopting a material approach to ESG makes particular sense; when resources are limited, it is critical to concentrate efforts on the issues that truly drive the company’s financial growth and its long-term economic and environmental sustainability.

For instance, a fintech or digital health startup might find that data security and privacy are the most material ESG issues, as they directly affect customer trust and regulatory compliance. On the other hand, a biotech company may prioritise issues related to ethical sourcing of materials or the environmental impact of production processes. Both are valid ESG concerns, but each is material to the specific context of the startup in question.

Materiality in action: Making ESG “Go Away”

When done well, materiality makes ESG “go away”—in the sense that ESG no longer feels like an extra external imposition or a compliance burden. Instead, it becomes integrated into the core decision-making process, aligned with other strategic and operational priorities like hiring, product development, and market expansion. This shift moves ESG from a compliance-driven activity to a strategic business consideration.

An early stage startup, for instance, might focus ons hiring a diverse and experienced team, which would not only be aligned with ESG but also strengthens the startup’s foundation for expansion. As the company scales, environmental factors like measuring and managing one’s carbon footprint may become more material e.g. for its B2B sales, prompting the company to adapt its strategy accordingly.

Continuously updating one’s materiality assessments as one scales, expands and pivots, helps triage time and resources, a crucial factor for both startups and VCs.

The bottom line

Through its community of 500 VC funds and 100 limited partners, VentureESG works to identify the key principles of doing ESG ‘right’, and at the heart of this is materiality. A materiality-focused approach to ESG is both the responsibility of VCs - in their due diligence and portfolio support efforts - and startups - in the day-to-day running of the business . Prioritising financially-impactful ESG issues makes good business sense for both parties.

Startups that ensure their ESG efforts reflect material concerns will help build resilience and long-term viability - and these benefits will be shared. Investors also gain from more informed decision-making during the investment process, identifying both opportunities and risks that could make or break a company. By working together on material ESG factors, founders and investors align around shared strategic priorities, leading to clearer communication and greater efficiency in execution. *Our recently published case studies* from 27 funds in our membership, including Balderton, Atomico, HV Capital and Base10, provide compelling evidence of the win-win potential that effective ESG can unlock.

Take diversity, equity and inclusion, for example. Hiring a team of decision makers with diverse skill sets or investors from underrepresented backgrounds, coupled with building a strong inclusive culture - empowering talent to speak up, compensating them equally - is beneficial; it will not only make for more well-rounded decisions but will likely lead to for lower turn-over and higher team satisfaction. DEI is material *for both VCs* and *many companies*. Likewise, governance issues have been at the core of major startup failures, from WeWork to FTX, proving that focusing on governance as a material ESG issue isn’t just compliance, it’s smart risk management.

The most valuable advice VCs can offer startups is this: “If you want to do ESG right, start with materiality—and watch it become part of your company’s DNA.”

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