WHITE PAPER

Airports, ESG and Securing Aviation's Permission to Grow

Airports understand that their permission to grow and operate relies on two key factors: a commitment to sustainability and demonstrable efforts to reduce, eradicate or mitigate the impact of their operations on the environment and communities they serve.

Being a so-called 'good neighbour' isn't enough, however. As a greater focus on the role of business in confronting wider societal issues has become prevalent, the business imperative for airports to develop and adopt a more comprehensive approach to environmental, social and governance ("ESG") issues has become more important.

The widespread adoption of ESG across the world has been driven by two concurrent trends:[1]

- significant social pressure
- a growing recognition amongst investment and business professionals that ESG issues can have a material impact on company value.

It is accepted that managing such risks can preserve - and even enhance - economic value for companies.

A number of watershed moments have also increased the imperative for companies to take responsibility for issues that could affect the environment and society. The impacts of the global financial crisis, the Paris Agreement on Climate Change and the increasing focus on workplace issues have all affected the development of ESG management. This has led to increased scrutiny from communities, stakeholders and investors, as well as changes in regulation and new market initiatives to address systemic gaps in identifying and managing key risks.

Add to this the unprecedented economic and health crisis we are currently experiencing as a result of COVID-19, and it is clear the cost of inaction on ESG matters is now too high.

For airports, the potential risks are acute and wide-ranging, from losing a social license to operate and grow, experiencing employee retention problems in a constrained job market, to losing access to capital and non-compliance with incoming regulation.

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THE TRANSFORMATION OF THE AIRPORT BUSINESS MODEL

Historically, airports were predominantly government owned and often viewed simply as infrastructure providers. Over the last 25 years, however, this business model has changed fundamentally across much of the world with growing private investment and ownership in airports and an increasingly competitive market, especially in the Asia-Pacific.

Airports in the Asia-Pacific are now mature, sophisticated businesses and important economic engines imbued with a more assertive pursuit of growth and improvement. Changes in ownership and management have also resulted in a greater focus on corporate social responsibility, environment and sustainability issues focused predominantly on noise, air and groundwater quality, and emissions. They have also begun to adopt a more active approach to sustainability and community engagement, moving away from a siloed focus on environmental issues and embracing creative ways of engaging with local communities.

Growing investment in airports has inevitably resulted in increased scrutiny of sustainability and community impacts from investors and shareholders. This was recently illustrated by a major Australian pension fund placing large energy companies in the spotlight.[2] The pension fund was concerned about how well those companies' climate strategies align with efforts to hold global warming to 1.5 degrees Celsius above pre-industrial levels and how future capital expenditure will support the shift to a low-carbon economy.

As airports seek to attract greater levels of investment - and, indeed, many global pension funds have invested in airports around the world - there is a natural impetus to develop a more mature approach to addressing ESG risk 'in the round'. While social investment, community relations, green initiatives and corporate communications may be part of an ESG program, these efforts should not be misunderstood as representing the full scope of an airport's approach.

THE RUNWAY TO AN EFFECTIVE AIRPORT ESG STRATEGY

Based on our extensive work with businesses on ESG, we've found that a good ESG program includes a purpose-driven strategy that focuses on company-specific material issues and is fully integrated with the business objectives of the airport. It requires a conscious effort that is led by the board and management, which permeates the entire company, built on the following foundations:

- **Every ESG program should be rooted in materiality:** airports should regularly conduct an ESG materiality assessment which helps organise and prioritise relevant ESG factors based on their level of impact on the business and key stakeholders. When identifying material issues, airports should consider a long-term approach, which allows them to consider both direct and indirect financial impacts that may stem from social or environmental risks and opportunities.
- **Targets and reporting on progress are key:** once an airport identifies and prioritises material issues, it should set clear objectives and strategies for each key issue. This includes selecting metrics and KPIs, data collection and establishing challenging and realistic performance targets, followed by policies and initiatives. Robustness and transparency of disclosures and targets are key – a simplistic PR exercise will be immediately recognised and criticised as tokenistic and cynical.
- **Good governance drives performance:** the involvement of the board in driving oversight of the ESG strategy, supported by a cross-segment management team with clear ESG responsibilities, is crucial to demonstrate the seriousness of an ESG program. More importantly, to ensure that it is successful.
- **Ongoing evaluation secures long-term success:** airports must regularly assess their key material priorities and adjust their strategies accordingly. This requires a regular review of the materiality assessment as well as ensuring the current approach adopted follows best practice, from risk management to reporting and compliance.

In the end, airports should focus on addressing ESG risks unique to their business, going beyond compliance and being proactive.

No other business risk is addressed from a reactive perspective, so neither should ESG risk.

THE 'SEVEN SINS' OF ESG MISMANAGEMENT

Having successfully laid the runway for their ESG approach, airports must be wary of practices that may lead to missed opportunities. At best, this can result in failure to receive credit for their efforts but, at worst, can leave the company exposed to significant risks.

FTI Consulting has identified the following misconceptions and practices which can lead to significant pitfalls.[3] All stem from a lack of a purpose-driven strategy that focuses on company-specific material issues and is fully integrated with the business objectives of the organisation.

1. **Excessive focus on ratings:** an approach that focuses exclusively on improving the company's rating is at risk of allocating more resources to 'ticking boxes' instead of developing a strategy that is tailored to the company's unique outlook and exposure to risk. Positive ratings can indeed help a company gain recognition, but they should be viewed as only the outcome of the company's efforts.
2. **Treating ESG solely as a communications effort:** communication is a critical tool to help an airport amplify its messaging and airports now communicate with customers and communities with greater sophistication. Communications efforts cannot substitute for a robust management system that addresses material risks, however. Investors and other stakeholders can see through messaging that does not correspond to significant action - often referred to as 'greenwashing'.
3. **Lack of board and management oversight:** some companies delegate ESG or sustainability responsibilities to individuals or departments within the firm, without involving the board and senior management. It is imperative, however, that the board and senior management not only oversee but also champion the company's ESG strategy, bringing it to full alignment with the broader business strategy.
4. **Disconnect from business strategy:** an ESG strategy cannot be thought of separately from the airport's business strategy. Such disconnects may stem from potential misperceptions about the purpose of the ESG program, lack of board and management oversight, or a failure to conduct a thorough materiality assessment.
5. **Compliance-only approach:** to position themselves as leaders, airports need to proactively demonstrate best-in-class programs that go beyond simple compliance. They should exceed minimum requirements as part of a deliberate ESG strategy and fully explain their practices so they get full credit for their efforts.
6. **Inconsistencies across the firm:** failure to adopt an airport-wide strategy and achieve coordination across the business can lead to the inconsistent adoption of standards. This risk is especially prescient in an organisation with different business units. Airports are particularly susceptible to this and should seek to map their policies and programs across business units to facilitate the harmonisation of ESG efforts across the airport community. Fostering a consistent approach with equivalent practices on how to address material risks across airport partners is a crucial step.
7. **Lack of assessment and monitoring:** a lack of effective monitoring of ESG performance impedes an airport's ability to make progress and receive full credit for its ongoing initiatives through reporting. In addition to a review of data, the monitoring process should include continued assessment of the effectiveness of the company's programs, so that systems can be adjusted to achieve continuous improvements.

These 'sins' may not necessarily qualify as deadly, but they can prove dangerous if they lead to poorly managed or superficial approaches to risk management.

ADDRESSING THE ELEPHANT IN THE SUPPLY CHAIN

Individual ESG programs often treat their supply chains as separate from their own approach to key issues including carbon emissions, climate change risk, pollution, and human rights. For airports, there are many environmental and social risks that lie in their supply chains but are technically outside of their direct control. An airport's ESG plans might omit the actions of airlines, ground handlers, and others in the supply chain and retreat into the old approach of saying that these things are: 'out of our control'.

Aviation is an interconnected and interdependent ecosystem. Considering an airport's supply chain in its entirety when planning an ESG program ensures the business is able to give a robust indication to all stakeholders – including leadership – about actions taking place across the eco-system.

Airlines and other parts of the supply chain can be part of this conversation as more airports around the world attempt to take a whole-of-airport approach to sustainability.

ESG HAS LANDED

We have passed the point of no return in terms of ESG adoption; it has arrived. We have reached a 'new normal' where both companies and investors have begun to use it as a key differentiator and a tool for monitoring and managing risks. Indeed, as the world continues to plot a long-term and sustained recovery from the impact and effects of the pandemic, airports that are slow in evolving their ESG programs should expect tougher conversations in the future with their shareholders and other key stakeholders

As public opinion on social and environmental issues grows and is more receptive to increased scrutiny on businesses, companies, investors and other market participants are likely to become increasingly aware of the potential financial and reputational impacts of ESG management.

This is particularly important for airports as they fight to get back on the path to long-term growth and meet the returning passenger demand which is surging. The global association of airports, Airports Council International (ACI), predicts traffic levels will return to pre-pandemic levels within two to three years and will then double globally within the next two decades.[4]

The time is now for a more proactive approach to monitoring and managing ESG risks as airports plan the investment in people and infrastructure that meeting this surging demand will require.

FORGING AN ESG PATH WITH FTI CONSULTING

Some airports are well-advanced on their ESG journey, others are only at the beginning.

FTI Consulting can assist airports at any stage of their ESG journey by helping them develop an integrated program across all operations to draw together the various relevant business strands. Airports already gather data on environmental impact, community and stakeholder engagement, and their approach to workforce and governance, but transforming this into an integrated ESG approach is challenging.

Quantifying environmental action, creating integrated ways of benchmarking and reporting, and helping management teams make sense of the various reporting platforms and measures can be daunting for companies starting their ESG journey. FTI Consulting can assist through:

— **ESG assessments & due diligence:** taking a thorough approach from policy gap analysis to on-the-ground investigations will build a clear ESG profile.

— **Materiality assessments:** quantitative and qualitative analysis will identify factors that may have a material impact on the organisation.

— **ESG program development:** FTI Consulting helps clients evolve their ESG program, from strategy development to project implementation.

— **Sustainability reporting:** developing ESG narratives and disclosures that resonate with key stakeholders and align with prevalent ESG–related reporting frameworks.

— **Supply chain audits:** we employ blockchain technology to deliver solutions that provide secure, efficient, cost-effective and transparent programs for businesses committed to ethical supply chain practices.

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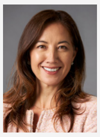
4. aci.aero/2022/10/06/the-impact-of-covid-19-on-airports-and-the-path-to-recovery/



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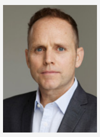

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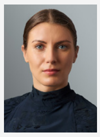

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