REDWOOD GROVE CAPITAL

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Fires, Air Quality and Climate

Some of my fondest memories as a child were snow days. Far superior to scheduled days off, they were filled with snowball fights, sledding, hot chocolate, and general foolishness. It was not until my wife and I had children and moved to the west coast that we experienced a different kind of school cancellation – one caused by smoke from wildfires burning hundreds of miles away. The smoke was so bad that school was not just canceled, our children were advised not to play outside at all.

This experience played a role in our family's decision to return to the East Coast, but of course our assessment was informed by a retrospective view of the world. As it turned out, New York was not immune from the effects of wildfires, and this summer was blanketed *again* by smoke, this time from Canadian wildfires. Fires burning hundreds or even thousands of miles away turned the sky hazy and made the air hazardous to breathe, reminding us that our world is more fragile than we often presume.

Wildfires are natural and, in many ecosystems, a necessary ecological process. However, the severity of a particular fire and its overall frequency depend on many interacting factors, one of which is climate change. The Intergovernmental Panel on Climate Change, a United Nations group that provides governments with scientific information they can use to help develop climate policies, concludes with high confidence that human-caused climate change has produced warmer, drier fire-weather conditions in North America and that these conditions have contributed to the increase in areas burned across the West. One influential study estimated that climate change was responsible for more than half of the observed increase in fuel aridity in western U.S. forests between 1979 and 2015, and nearly doubled the cumulative forest area burned from 1984 through 2015[1]. A quick shorthand is that for every 1 degree Celsius of warming, wildfires double in the American West.

Climate change does not cause every wildfire, but it increases the probability of longer fire seasons and fires that are larger and more difficult to contain. Higher temperatures increase the atmosphere's absorption of moisture, dry out vegetation and soils, reduce snowpack, and extend the portion of the year during which forests and grasslands are receptive to burning. The practical result is that an ignition is more likely to encounter unusually dry fuel, spread rapidly, and become difficult to suppress. It is not a coincidence that after a spring of record-breaking heat waves, France and Spain are currently experiencing the biggest wildfires in their history.

For investors, the distinction between cause and consequence is important. The world must continue working to reduce the emissions that intensify these conditions; however, communities are increasingly forced to adapt to a level of wildfire risk that is already present. That will require more resilient electric and water systems, improved emergency planning, and greater investment in the equipment used to prevent, contain, and extinguish fires.

Redwood Grove does not invest on the assumption that a bad fire season will produce a short-term earnings windfall. Municipal purchasing cycles are long, individual fire seasons are unpredictable, and emergency budgets remain subject to political and financial constraints. Rather, we believe that a persistent increase in physical risk will gradually influence how communities allocate capital. Fire departments will need to modernize aging fleets, utilities will spend more to protect and harden their

[1] http://pnas.org/doi/10.1073/pnas.1607171113

networks, and governments will devote greater resources to prevention, suppression, and recovery. In other words, their revenue tied to these firerelated businesses will continue to grow and become more durable over time.

These are examples of what climate adaptation looks like as an investment theme. It is not one product or one narrowly defined industry. It is a growing need for durable equipment, critical components, resilient infrastructure, and specialized services. The best positioned companies to meet that need may benefit over many years, not because fires are desirable (they are not), but because preparation for a changing physical environment is becoming economically unavoidable.

Closing Thoughts

I recently had the opportunity to sit down with Admiral James Stavridis. His résumé is almost overwhelming in its distinction. A former four-star admiral and Supreme Allied Commander of NATO, he has led through conflicts and crises spanning Afghanistan, Libya, Syria, and the Balkans. Given that experience, I was curious to hear what he viewed as the greatest risks facing the United States today.

His clear-eyed answer centered on three challenges: the growing tension between the United States and China, artificial intelligence, and climate change. I was struck that someone who spent much of his career confronting traditional military threats identified climate change as one of the nation's most significant security risks. In his view, its consequences extend well beyond the environment, affecting geopolitical stability, migration, food and water security, infrastructure, and economic resilience.

That perspective closely reflects Redwood Grove's investment philosophy. We believe the economic consequences of climate change remain broadly misunderstood and frequently mispriced by the market. Our approach is not limited to investing in companies traditionally labeled as "climate solutions." We seek durable businesses across sectors that are helping the economy mitigate climate change, adapt to its effects, or operate more effectively in a world increasingly shaped by resource constraints, physical disruption, and policy change. Admiral Stavridis's comments were a reminder that climate change is not a narrow thematic issue, but a structural force influencing economies, industries, and capital allocation for decades.

We are also pleased to announce that David Bluestein is joining Redwood Grove to lead our business development efforts. David has spent much of his career advising institutional investors and allocating capital on their behalf. Most recently, he served as a Senior Investment Consultant at Mercer. His experience and perspective will be valuable as we continue to build the firm and deepen our relationships with current and prospective investors. We look forward to introducing him to all of you in the coming months.

Thank you for your continued trust in our team and our process. As always, please reach out with any questions or thoughts.

With gratitude,

Ted

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