January 5, 2026

Dear Clients and Friends,

The idea was so big and simple – obvious, even – that there seemed no way, in the heady early days of the Internet, for it to fail. Global Crossing, founded in the wake of Netscape's wildly successful 1995 initial public offering, would create a global telecommunications network, enabling faster and cheaper communication by laying fiber-optic cable across the world and displacing older, slower satellite and copper wire systems. The company's network was seen as the physical backbone of a new global economy that would lower the cost of communication and unlock global commerce. Propelled by fawning press coverage and bullish investor sentiment, Global Crossing raised $400 million in its 1998 IPO and issued more than $20 billion in debt to fund construction of its network.[1] The technology worked: the submarine fiber-optic cables are still in service today and its network architecture remains the model for digital connectivity. However, capacity exceeded demand and revenue was insufficient to service the company's debt-laden capital structure, forcing Global Crossing into bankruptcy in 2002.[2]

The collapse of Global Crossing was a financial failure, not a technological one, another chapter in the economic history of innovations from canals to railroads, the automobile and smart phones – all of which benefitted humanity even as much of the early capital invested was lost. The Erie Canal, an engineering wonder completed in 1825 that established New York as a continental epicenter, fell short of its commercial promise when railroads proved a more efficient shipping method. Alas, railroads were equally perilous for early investors as debt-financed overbuilding resulted in bloated balance sheets, withering price competition and declining returns on capital. The automotive industry experienced a similar investor mania: in 1910 there were more than 250 car companies in the U.S., a universe that eventually consolidated into three large manufacturers, two of which ultimately filed for bankruptcy.[3] Despite the transformative innovation of the automobile, shareholder returns in the industry have been abysmal. First generation smart phones, including Palm Pilot, Blackberry and Nokia, were obliterated by Apple's iPhone, a late entrant to the market, while Google, with its superior search algorithm, displaced the early Internet browsers Netscape, AOL and Yahoo.

The cycle of creation and destruction that defines capitalism is most evident at the frontier of innovation, where investment swarms to the next big idea, often failing to discount emerging risks. From railroads to the Internet, history reveals that transformative inventions reshape society while transferring much of the economic benefit from investors to the broader economy.

**"The biggest mistake people make is thinking the way to success is through consensus"** – Steve Jobs

It is hard to know whether investors in the companies developing artificial intelligence (AI) are doomed to experience the same reckoning as early backers of America's industrialization but the margin of safety for the most highly valued companies seems thin. After returning 13x in the past three years, Nvidia is now worth more than India's entire stock market and represents 8% of the S&P 500, an index weighting attained only once before, by Apple in 2023.[4] OpenAI's next financing round may value the company at more than $800 billion, or 60x estimated revenue, with an IPO expected soon. Markets are starting to question whether the capital raised to develop AI will earn

[1] *APA-OTS / PR Newswire: https://www.ots.at/presseaussendung/OTS_19980817_OTS0026/global-crossing-completes-399-million-initial-public-offering-ipo-consisted-of-21000000-shares-priced-at-19-per-share-company-has-been-listed-on-nasdaq-and-bermuda-stock-exchange*
[2] *Investopedia: https://www.investopedia.com/terms/g/globalcrossing.asp*
[3] *https://www.assemblymag.com/articles/85688-gm-centennial-the-world-in-1908*
[4] Bloomberg L.P.

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adequate rates of return, as evidenced by soaring prices for credit default swaps on debt issued by Oracle and Softbank Group and awareness that competing technologies may emerge. Nvidia's customers, including Google and Amazon (with their TPU and Tranium custom chips, respectively), have the financial and technological resources to become competitors, potentially threatening Nvidia's perceived invincibility and margins. Instead of investing in companies whose success depends on sustained scarcity in technologies designed to become abundant, we seek investments with wider margins of safety.

We believe our long-standing investments in **Alphabet** and **Microsoft** are among the safest ways to gain exposure to AI, although both are investing heavily (with uncertain paybacks) and their valuations discount some of the gains we anticipate in the quarters ahead. Ultimately, we believe the winners will not be the companies selling AI itself, but those embedding it into workflows that customers rely on and are reluctant to abandon. Advanced computing, pattern recognition, and automation will help companies improve forecasting and decision making, which should enhance margins for companies with complex operations, such as **Costco** and **UBER**. Similarly, businesses with established customer relationships and pricing power, such as **Fastenal** and **Mastercard**, may find that AI strengthens rather than disrupts their competitive positions and protects existing economics. Our investment team seeks companies with durable competitive advantages, high returns on equity, prudent capital allocation, and the ability to adapt as new tools become available. Patience, selectivity, and a disciplined focus on intrinsic value will serve our clients well in the volatile economic environment we see ahead.

**"When government intervenes in markets, the benefits are concentrated while the costs are diffused."** – Martin Feldstein

Enthusiasm for the most popular stocks is driving inflows into passive investment products, amplifying the valuation disparity between the largest technology stocks and many others. At year end, the S&P 500 traded at 23x forward earnings and roughly 40x trailing cyclically adjusted earnings (the "CAPE ratio"), levels comparable to those reached in 1999.[5] The Buffett indicator, which compares the market capitalization of U.S. stocks to GDP is 220% (greatly exceeding its historical average), implying mediocre returns for the broad stock market averages.[6] Tellingly, gold and the S&P 500 both hit record highs at year end, a coincidence that happened in 1973 and 2007, years that marked stock market peaks.[7] Extended valuations can exist for a long time and, by themselves, do not suggest a market correction is imminent. In the context of today's economic climate, however, we believe caution is warranted as risks are evident in assets from lesser quality stocks to long-term bonds.

As the Supreme Court deliberates the legality of the government's tariff policy, history has already rendered its judgement that protectionism erodes national wealth by raising costs for consumers, restricting supply, and squelching innovation, as companies weigh commercial considerations against political imperatives. The benefit of tariffs to a small number of less competitive companies is dwarfed by the costs imposed on many. A parallel concern is the government's expanding role in the private sector by demanding "golden shares" in companies and royalties on exported products, such as advanced microchips. The administration's transactional economic policy complicates strategic planning for companies and undermines business confidence as those closest to power sometimes stand to benefit financially from policy decisions. As government redefines its relationship with private industry, deficit spending continues unabated. Annual interest expenditures on the $38 trillion in outstanding

[5] https://shillerdata.com/
[6] Bloomberg L.P.
[7] Bloomberg L.P.

Treasury debt exceeds outlays for national defense.[8] Some suggest the government should have a role in setting interest rates, challenging the principle of Federal Reserve independence – a theory we believe puts at risk the role of the Dollar as the world's reserve currency and the resulting structurally low interest rates that arise from capital inflows. The cumulative effect of these policies seems muted for now but elevated inflation, subdued corporate investment, and higher long-term interest rates are plausible outcomes.

**"Choose your heroes very carefully and then emulate them"** – Warren Buffett

Articulating economic risks does not mean we believe investors should sell stocks; to the contrary, excesses in certain asset classes create opportunities elsewhere. The best opportunities we see now are in quality common stocks, defined by recurring revenue, sustained pricing power, shareholder-oriented management teams, and fortress balance sheets.

**Amazon** and **Berkshire Hathaway** exemplify these attributes. Amazon's formidable moat is built on the immutable truth that customers will never wish for higher prices or slower shipping. Amazon has created the world's best delivery network, which should become increasingly profitable as the company expands internationally. Despite producing market-trailing annualized returns of less than 8.0% over the past five years, we believe capex will moderate next year, resulting in sharply higher free cash flow growth.[9] Similarly, Berkshire's common stock has been weighed down by management succession, an array of businesses relatively less exposed to AI and a balance sheet anchored by more than $350 billion in cash.[10] Currently, Berkshire trades at 1.4x estimated book value, a measure we believe understates intrinsic value as GAAP accounting obscures the company's true economics.[11] Berkshire's recent investments in public stocks have been unremarkable and small – and we expect the company under new CEO Greg Abel to deploy its vast cash reserves in share repurchases or acquisitions in 2026.

Discussion of Berkshire is incomplete without noting the retirement of Warren Buffett, the intellectual mentor to our firm. Early pilgrimages to Omaha for Berkshire's annual meeting bound our nascent partnership together in a shared vision for quality value investing and a commitment to make our clients' interests paramount. In his Thanksgiving letter to shareholders, perhaps among the last he will write, Buffett put his wealth and investment acumen in perspective by noting, "Greatness does not come about by accumulating vast amounts of money…, publicity or power in government. When you help someone in any of thousands of ways you help the world."

Building on the firm's continued growth and long-term vision, we are pleased to announce the addition of Ted Crawford to the firm's partnership this year. As a new year begins, we pledge to keep Warren's counsel in mind and express our gratitude for the steadfast support of our clients and colleagues, who made 2025 a record year for our firm.

Sincerely,

Douglass Winthrop Advisors LLC

[8] *https://www.cbo.gov/publication/61307*
[9] Bloomberg L.P.
[10] Berkshire Hathaway SEC Filings
[11] Bloomberg L.P.