April 9, 2024

Dear Sustainable Equity Strategy Clients and Friends:

Eleanor Creesy understood the crucial difference between weather and climate, and wondered if she could somehow act on it. She knew weather was a capricious mix of shifting currents, while climate manifested in longer term patterns…if only they could be divined. As navigator of the clipper ship *Flying Cloud* in 1851, a time when the speed to destination of sailing ships was reported on newspapers' front pages, Creesy knew that her bottom line and her reputation depended on her speed from New York to San Francisco. The California Gold Rush was in full swing and the first to market with supplies or passengers commanded a premium.

Sailors back then did their best with "dead reckoning," an imperfect art of determining their position from a previously known position plus complex calculations of direction and speed while accounting for the influence of currents and wind on drift. Shifting breezes and currents often added days or weeks to a voyage, causing anxiety among shippers, owners, sailors and underwriters. Creesy knew she needed to innovate to justify the unprecedented price the owners had paid for *Flying Cloud*. And that's exactly what she did…

Creesy had grown fascinated by the work of Matthew Fontaine Maury. In perhaps the first 'Big Data' project in history, Maury had discovered a forgotten storage depot in Washington, D.C. containing thousands of old ships' logs and charts going back to the start of the U.S. Navy – a potential mother lode for discerning elusive climate patterns. Maury built a team to collect and systemize the long-forgotten data on winds, calms and currents across all seas and seasons. Under his leadership, the old depot became the United States Naval Observatory and the climate work he pioneered was slowly adopted by sailors around the world – earning him the moniker 'Pathfinder of the Seas.' Eschewing traditional navigation precepts, Creesy harnessed Maury's data to plot a novel course for the *Flying Cloud* – one that would take advantage of prevailing winds and currents, while minimizing the time she spent in the dreaded Doldrums. This innovation in climate science ultimately enabled her to reach San Francisco in 89 days, a sailing record that stood for 138 years.[1]

As managers of the Sustainable Equity Strategy (SES), we are aligned with Eleanor Creesy. Our role on your behalf is to look past the short-term caprice of market fluctuations and instead assess how the long-term arc of climate and other secular drivers affect the economic prospects of businesses. The crucial data is no longer stored at Maury's depot or any other dusty repositories. Rather we are now able to turn to advanced climatology and other earth sciences to inform our navigation of markets in the "Anthropocene" — an epoch during which human activity has become a powerful, even dominant, influence on our climate and other planetary resources. The challenge of feeding, clothing and providing energy to a large global population amidst this dynamic era requires the wise and increasingly optimized use of shared resources. The urgency of this task becomes clearer by the day: the "tragedy of the commons," or the impact of often remote actions by others on our planetary support systems, is playing out across sectors and geographies, with important implications for investing. Examples abound.

Climate Change, the Panama Canal and Portfolio Construction

The Panama Canal is highly dependent on rainfall to function as one of the world's most important shipping channels. The Canal currently is enduring one of the most severe droughts in recorded history. According to the Peterson Institute, accelerating change in the region's climate is raising doubts about the Canal's long-term viability.[2] An issue ominous to the future of the Canal may be at work. The Amazon rainforest produces its own rainfall, generating a self-sustaining cycle that also moderates the regional and global climate. Deforestation can

diminish the rainforest's ability to sustain itself, resulting in reduced rainfall locally and regionally, including at the Canal.[3] We may well have reached that point.

Economists observing this would say that the market has failed to price or “internalize” the real cost of logging the Amazon. Rather the loggers impose those costs on others. In response, the Panama Canal Authority has raised toll rates and restricted by a third the number and size of vessels that can transit through the Canal, leading to soaring shipping costs. A failing Panama Canal threatens global trade, especially U.S. exports and imports. Less rain also harms agriculture and encourages emigration. These factors exacerbate inflation and threaten regional and national security. A casual observer might think these “true” costs outweigh the value of the timber harvested.

The premise of the SES is that climate change, water stress, resource scarcity, soil degradation and deforestation influence long-term investment returns just as much as future interest rates, inflation, recessions or other closely watched (and usually shorter term) financial factors that more typically preoccupy investors. The costs of these environmental impacts are being internalized over time, unevenly but often materially, through such mechanisms as changes in consumer tastes, regulations, and technology. These responses become reflected in the reinforcing mechanism of prices, and thereby drive trends in capital allocation and investment. We believe, therefore, these factors should play a material role in investment decisions.

Most investors lack the focus or domain expertise to handicap environmental factors and their first and second-order implications. As a result, we believe that such opportunities and risks are sometimes improperly priced in the equity markets. In a world of nearly ubiquitous information driving a more level playing field for investors, understanding the influence of environmental factors on a business can lead to a differentiated view of its long-term prospects and possibly provide investors an opportunity to outperform the general market. During the first quarter of 2024, our Strategy returned 10.48% gross / 10.25% net of fees. More relevantly given our long-term horizon, we have completed a 7.25-year track record, returning 17.18% gross / 16.12% net of fees, annualized since inception, which puts the Strategy’s performance ahead of our reference indexes. Please see page 4 for a more complete performance table. (Past performance is no guarantee of future results).

Our SES team continuously invests in enhancing our personnel and process to integrate environmental factors and economic fundamentals to better inform our investment decisions. In Q4 of 2022, after an exhaustive search we hired Michael Marciante as a new research analyst. Michael comes to us after serving as an analyst across multiple business segments at UBS Asset Management and has hit the ground running. As part of our investment process, we continue to refine our “E-Map,” which guides our view of the surprisingly large opportunity set in such sectors as transportation, agriculture, construction, waste management, water quality, precision agriculture, human health, industrial efficiency, finance, and information technology. Select investment ideas generated from our E-Map are evaluated against our proprietary “E-Assess” process to identify and understand overlooked environmental factors that can have a material positive or negative impact on a business’s prospects over the long term.

We marry these findings with a bottom-up assessment of the same core business attributes that Douglass Winthrop Advisors has evaluated since its founding 25 years ago: a strong competitive moat; attractive opportunities to reinvest in the business to compound returns; shareholder-oriented management; financial strength and resilience; and a reasonable valuation. This methodical and repeatable process results in a portfolio characterized by two types of companies: those whose core business strengths are materially augmented by environmental advantages (E-Advantaged), and those whose core business offers solutions to intensifying environmental challenges and are therefore poised, we believe, to grow at above-market rates (E-Solution Providers).

E-Advantaged and E-Solutions Holdings: Aon and Brookfield Asset Management

Eleanor Creesy's innovative use of long-term climate data to capture an edge over her less innovative competitors offers an example of an E-Advantaged business. Since 1851, the value of climate data has only continued to grow as planetary change accelerates. The insurance sector is on the front line of meeting this challenge. Global insured loss due to natural catastrophes has averaged $100 billion over the last five years, according to Verisk -- an increase of about 40% over the previous five. Verisk attributes this growth to two causes: inflation and climate change.[4] The firm estimates that current insured claims for natural catastrophes could exceed $130 billion per annum, and that only about 25% of the annual cost of natural catastrophes are presently covered by insurance. Not only does this indicate a large opportunity for the insurance industry, but it also highlights the importance of correctly pricing underwriting exposures. Our holding **AON**, which importantly takes no underwriting risks itself, is a leading risk advisor and insurance broker to global corporations, and also counsels insurance and reinsurance companies whose underwriting models must be updated to cope with climate change. AON has, we believe, materially widened its competitive moat by incorporating industry-leading climate tools into its offerings. AON's Climate and Resilience Hub is a focal point for its climate expertise for delivering climate and resilience solutions to companies as they contend with mounting regulatory, investor, consumer, employee, and operating pressures. AON's management team believes there is a rapidly growing opportunity to assist companies, municipalities and even countries in planning for an orderly and efficient transition to a more sustainable and productive economy.

Our holding **Brookfield Asset Management** (BAM) has diversified its fast-growing alternative asset management business by investing in decarbonization, and related secular themes such as digitalization and deglobalization of supply chains. Custom Market Insights estimates that the annual investment in decarbonizing the global economy will grow at annual rate of 11.5% to $2.5 trillion by 2032.[5] BAM has taken note. It raised $93 billion in new capital during 2023 and closed the year with $457 billion of fee bearing assets under management, giving it the scale to match large pools of capital with opportunities in the global economic transition. Its renewable power platform owns and operates one of the world's largest fleets of clean energy and energy-transition assets, having deployed over $100 billion.[6] In 2023, it reported 25 Gigawatts (GW) of renewable power under management with a backlog of 110GW under development. BAM has made a net-zero commitment by 2050 for reducing its greenhouse gas emissions, covering its investments in electricity transmission and distribution, telecommunications and data centers, manufacturing and construction services, transportation, and supply chain resilience. A world in need of more efficient, reliable and resilient infrastructure leaves BAM with no shortage of opportunities to profitably deploy capital and positions it as a financial E-Solutions behemoth.

Performance

The 2023 boost to equity markets from artificial intelligence (AI) continued in Q1, and the SES benefited from this trend. It took Matthew Maury and his revolving team of Navy personnel many years to divine useful secrets from the thousands of old ships logs he found. AI is now doing that kind of work in milliseconds, with profound implications for our ability to solve, mitigate and adapt to environmental change. AI tools are being developed to improve planning and risk management. These tools allow for on-the-fly route optimization, inventory control, demand forecasting and inspire productivity improvements. Efficiency gains promise reduced energy use and increased business model resilience. Forward-looking companies are investing heavily in AI tools to cut costs, drive revenue and make operations less vulnerable to disruption. These investments, in turn, are generating demand for additional capacity in communication networks, data storage and processing, smart grids and industrial automation.

Digital applications to the multi-trillion-dollar transition economy are a key segment of our E-Map, and we continue to monitor opportunities up and down the information technology value chain. Two of the leading picks-and-shovels companies enabling AI advances were significant contributors to SES performance in Q1. A formidable operator, **Taiwan Semiconductor** (TSM) makes 90% of Nvidia's advanced chips for AI and 60% of all semiconductor chips globally.[7] Likewise, our holding **ASML** is the only company in the world building the Extreme Ultraviolet lithography (EUV) machines that TSM, Samsung, Intel and others use to manufacture advanced chips. Its latest generation chipmaking machines cost about $380 million each.[8] Given this competitive positioning and pricing power, we believe ASML will generate high returns on capital for many years to come.

In the first quarter of 2023, we chose to sell longtime holding **Costco** and harvest gains for redeployment to other opportunities. Costco continues to execute beautifully on its advantaged business model and is making strides on a more aggressive climate action plan, in part due to a shareholder resolution which we voted for in early 2022. Our internal modeling, however, suggested that even rosy, bull-case scenarios of future performance were already priced into the rapidly accreting stock price. Cognizant that U.S. equity markets are more expensive than most international markets on a variety of valuation metrics, in Q1 we bought positions in two burgeoning e-commerce businesses domiciled and serving markets outside of the United States. We believe these companies have carbon-advantaged business models and will discuss them in more depth in a future letter. **Nike** was a negative contributor to performance during the quarter. While Nike is one of the world's most valuable global brands, its pivot to a direct-to-consumer (DTC) channel has faltered while also distracting management from its once formidable product innovation machine. We trimmed our Nike position before its release of Q4 earnings last month and continue to evaluate management's plans for re-accelerating growth while fending off increased competition.

			Reference Indexes		
	DWA Sustainable Equity (gross)	**DWA Sustainable Equity (net)**	**MSCI SRI TR Index**	**S&P 500 Total Return Index**	**MSCI World TR USD Index**
Annualized Returns					
1Yr	24.59%	23.59%	22.51%	29.88%	25.07%
3Yr	8.07%	7.15%	8.62%	11.49%	8.59%
5Yr	15.66%	14.65%	13.17%	15.05%	12.07%
Inception	17.18%	16.12%	12.79%	14.50%	11.64%
Cumulative Returns					
1Yr	24.59%	23.59%	22.51%	29.88%	25.07%
3Yr	26.20%	23.01%	28.17%	38.59%	28.06%
5Yr	106.94%	98.11%	85.61%	101.57%	76.76%
Inception	215.66%	195.60%	139.23%	166.86%	122.15%

Inception date: January 1, 2017

Past performance is no guarantee of future returns.

In closing, we thank our clients for entrusting their capital to us during this time of profound transition. Your continued confidence strengthens our resolve. We believe the SES portfolio is built for long term resiliency and growth. If you'd like to set up a call or to visit the team, please be in touch with either Dan Abbasi at dan@douglasswinthrop.com or Bowdy Train at bowdy@douglasswinthrop.com. We welcome your inquiries.

Best regards,

The Douglass Winthrop Team

Please see endnotes and important disclosures below.

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1 https://no-frills-sailing.com/flying-cloud-clipper-ship-book-david-m-shaw/

2 https://www.piie.com/blogs/realtime-economics/2024/panama-canal-may-dry-because-amazon-deforestation

3 https://www.eia.gov/todayinenergy/detail.php?id=60842

4 https://w4.air-worldwide.com/Global-Modeled-Catastrophe-Losses-2023

5 https://www.custommarketinsights.com/report/decarbonizing-market/#:~:text=As%20per%20the%20current%20market%20research%20conducted,is%20anticipated%20to%20reach%20USD%202544.1%20Billion.

6 https://www.wsj.com/finance/investing/the-investment-firm-that-keeps-raising-giant-climate-funds-9ef4ecad

7 https://www.ft.com/content/89745f19-1968-4c46-aaf2-5c6a6a50067f and https://www.economist.com/special-report/2023/03/06/taiwans-dominance-of-the-chip-industry-makes-it-more-important

8 https://www.techpowerup.com/319071/asml-high-na-euv-twinscan-exe-machines-cost-usd-380-million-10-20-units-already-booked#:~:text=The%20hefty%20$380%20million%20price,also%20necessitates%20rethinking%20chip%20designs.