

Q4 2018 Earnings Call

Company Participants

- Dave Bonham, Chief Financial Officer
- Derek Bulas, Legal Counsel
- Paul Rivett, President

Other Participants

- Andrew Hollingworth, Analyst
- Daniel Chan
- Howard Slinker, Analyst
- Jaeme Gloyn, Analyst
- Jeff Fenwick, Analyst
- Junior Ross
- Mark Dwelle, Analyst
- Mikel Abasolo, Analyst
- Paul Holden, Analyst
- Tom MacKinnon, Analyst
- Unidentified Participant

Presentation

Operator

Good morning and welcome to Fairfax 2018 Year-End Results Conference Call. Your lines have been placed in a listen-only mode. After the presentation, we will conduct a question-and-answer session. (Operator Instructions). Today's conference is being recorded. If you have any objections you may disconnect at this time.

Your host for today's call is Paul Rivett, with opening remarks from Mr. Derek Bulas. Mr. Bulas, please begin.

Derek Bulas

Good morning, and welcome to our call to discuss Fairfax's year-end 2018 results. This call may include forward-looking statements. Actual results may differ, perhaps materially, from those contained in such forward-looking statements as a result of a variety of uncertainties and risk factors, the most foreseeable of which are set out under Risk Factors in our Base Shelf Prospectus, which has been filed with Canadian Securities regulators and is available on SEDAR.

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I will now turn the call over to our President, Paul Rivett.

Paul Rivett {BIO 15243791 <GO>}

Thank you, Derek. Good morning, Fairfax shareholders. Welcome to your company's 2018 year-end conference call. I will discuss some of the year end highlights, and then pass the call to Dave Bonham, our Chief Financial Officer for additional financial and accounting details.

Fairfax's net earnings were \$376 million in 2018 versus \$1.7 billion in 2017, which equates to net earnings per diluted share of a \$11.65 versus \$64.98 in 2017. Much of this year-over-year net earnings difference relates to unrealized investment losses and the sale of First Capital.

Fairfax's book value per share in 2018 decreased by 1.5% adjusted for the \$10 per share common dividend paid in the first quarter of 2018 to \$432 per share. Despite having earnings for the year, our book value was negatively impacted by unrealized foreign currency translation losses of \$11 per share.

We experienced another year of above average catastrophes, yet our companies continue to have very good relative results with a strong combined ratio of 97.3% across the Group, with strong reserves and producing an underwriting profit of \$318 million for the year. All of our major insurance companies with the exception of Brit generated combined ratios of less than 100%, with Zenith at 82.6%, Odyssey Group at 93.4%, Northbridge at 95.8% and Allied World at 98.1%, Crum & Forster at 98%, while Brit was 105.2%.

For the year, operating income was strong at nearly \$1 billion. By contrast, our net gains on investments for the year were an unsatisfactory \$253 million consisting of realized gains on our investment portfolios of \$1.2 billion principally Quess, USG, Arbor and Intrepid offset by unrealized losses of just over \$900 million, principally BlackBerry, Eurobank and Stelco, most of which occurred in the fourth quarter. As we have mentioned that our annual meetings and in our annual reports and quarterly calls, with IFRS accounting where stocks and bonds are recorded at market and subject to mark-to-market gains or losses. Quarterly and annual income will fluctuate and investment results will only make sense over the longer term.

The turbulent markets in the final few months of 2018 wreak havoc on investment portfolios globally. Our portfolios were similarly impacted but we fared better than many. Much of this turbulence has reversed in the early weeks of this new year and investment asset prices have generally risen. At Fairfax, our top 20 listed equity investments dropped approximately \$500 million in value in just the fourth quarter. But since the end of the year, our top 20 equity positions have recouped over 50% of the decline..

Please keep in mind when you see these short-term mark-to-market gyrations, as we have said many times in the past, our results will be lumpy as we are focused on capital preservation in the short-term and capital gains over the long term. There are some key

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points to note for you. Strong organic growth is continuing at our companies. Our insurance and reinsurance businesses' net written premium increased year-over-year by 8.7%, primarily due to growth at Northbridge, Odyssey, Crum & Forster and Brit after adjusting for acquisitions and the sale of First Capital.

At the subsidiary level, the change in net premiums written for the year were as follows: Odyssey Group was up 16.1%; Crum & Forster up 6.1%; Northbridge up 10.2%; Zenith was down 5.8%; Brit up 9%; and Allied World up by 5.8%. In 2018, we continue to put more of our cash to work with approximately \$13 billion invested in short-term U.S. treasuries and short-term investment-grade corporate bonds. Given the continued strength in the U.S. economy and the perceived bias towards higher interest rates, we continue to be focused on the short end of the treasury curve for the time being.

Following this recent deployment in the short-term U.S. treasuries, we now have an annual run rate of approximately \$800 million in interest and dividend income. Subsequent to the end of 2018, in January of this year, we invested an additional \$250 million in debentures of Seaspam, as well as \$250 million in the exercise of Seaspam warrants. Upon completion of these transactions, our cumulative cash investment in Seaspam totaled \$1 billion.

In February, we completed an opportunistic offering of \$85 million in senior notes due in 2024 with our partner, Mitsui Sumitomo. We continue to build on the strong trusting relationship with MSI and see the potential for many more collaborative business ventures in the future. Last week, the shareholders of AGT approve the management led take private transaction. AGT as a Regina based world-leading supplier of plant-based proteins. We welcome AGT to the Fairfax family and we look forward to collaborating with our new partners Murad and Hussein, and their teams to continue to build our respective agricultural businesses around the world.

Also last week, we announced the promotion of one of our key executives Peter Clark, the Vice President and Chief Operating Officer. Peter has been with Fairfax for over 20 years in various roles, such as Chief Actuary and more recently, our Chief Risk Officer. Peter will report directly to me and will continue to work very closely with Andy Bernard and the CEOs of our insurance and reinsurance companies.

We remain conservatively positioned and very vigilant with holding company cash and marketable securities at over \$1.5 billion. Always looking to be soundly financed first, we have begun to repurchase our partner's interest in our insurance companies, as well as repurchasing Fairfax shares. Since the first quarter of 2017, we have purchased over \$1.1 million Fairfax shares with approximately 340,000 shares purchased in the last six weeks alone. Our investment team at Hamblin Watsa continues to cautiously observe and monitor events, such as the upcoming U.S. elections, Indian elections, South African elections, the Venezuelan crisis, Brexit negotiations and ongoing negotiations on global tariffs in particular with China.

Please remember, we continue to hold CPI-linked to deflation for contracts with a notional amount of \$114 billion and an average remaining term of maturity of 3.6 years. We carry these contracts at only \$25 million and they continue to provide us with downside

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protection in the event of a catastrophic turn of world events. With annual run rate of approximately \$16 billion in gross premium, generating strong core operating earnings and a singular focus on underwriting discipline and superior reserving, our companies are in a very good position to continue growing and diversifying their books of business, while capitalizing on the potentially hardening market.

Meanwhile, the Hamblin Watsa team continues to believe there is tremendous opportunity for Fairfax shareholders over the long term. We are keenly focused on improving our investment performance in 2019 and we are in the process of monetizing many of our equity investments. We believe our 15% return on equity target is very much achievable, but please remember, as we've said before, our results will always be lumpy. While we monetize our equities and reoptimize our portfolio, we have not reach for yield and we made prudently invested with approximately \$20 billion in cash, short-dated U.S. treasuries and short-dated investment grade bonds, which is approximately 53% of our portfolio investments. Given the short tenure of our fixed income portfolio, our investment portfolios will be largely unimpacted by rising interest rates.

Now I'd like to pass the call over to Dave Bonham, our Chief Financial Officer.

Dave Bonham {BIO 15243784 <GO>}

Thank you, Paul. First of all, we wanted to let you know that in addition to the press release that we issued yesterday, all of the details of our 2018 financial results will be made available in our annual report, which will be posted on our website on March 8, 2019. So let's move on to Fairfax's consolidated results for the full year of 2018, hit on some of the details of the operating company results and finished with our consolidated financial position.

So for the full year of 2018, Fairfax has reported net earnings of \$376 million or \$12 per fully diluted share and that compared to net earnings of \$1.7 billion or \$65 per fully diluted share in the full year of 2017. 2018 net earnings principally reflected the strong operating income, but with lower net investment gains compared to 2017. And remember too, that our net earnings in 2017 also included a one-time gain of \$1 billion related to the sale of our Singapore-based subsidiary First Capital.

Our insurance and reinsurance operations produced an underwriting profit of \$318 million and a combined ratio of 97% in 2018 compared to an underwriting loss of \$642 million and a combined ratio of 107% in 2017. The increase in underwriting profit year-over-year of \$960 million, principally reflected the impact of lower current period catastrophes, since 2017 was adversely affected by Hurricanes Harvey, Irma and Maria and the 2017 California wildfires. Net favorable prior year reserve development was also higher in 2018 on a year-over-year basis.

Current period catastrophe losses in 2018 were principally comprised of the 2018 California wildfires, specifically the Woolsey and Camp wildfires and Hurricane Michael, which affected Florida and Southeastern United States, Typhoon Jebi, which affected Japan and Hurricane Florence. In 2018, current period catastrophe losses totaled \$752

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million representing 6.5 combined ratio points significantly lower than current period catastrophe losses in 2017 of \$1.3 billion that represented 14 combined ratio points.

Net premiums written by our insurance and reinsurance operations increased by 20% in 2018, but that principally reflected the consolidation of the full year net premiums written by Allied World. So that was an incremental year-over-year increase of approximately \$1.4 billion. In terms of our organic growth, net premiums written of the insurance and reinsurance operations increased by 8.7%, so that's after adjusting for the acquisitions of Allied World and the AIG branches in Latin America in Central and Eastern Europe, the sale of First Capital last year and some other one-off intercompany reinsurance transactions. All of these occurred either in 2017 or 2018.

So moving to our operating company results starting with Northbridge. Northbridge's underwriting profit increased to \$47 million in 2018 with a combined ratio of 96% that compared to an underwriting profit of \$9 million and a combined ratio of 99% in 2017. Northbridge's 2018 underwriting results included the benefit of net favorable prior year reserve development of a \$107 million representing 10 combined ratio points and that was somewhat higher than 2017 with Northbridge reported net favorable reserve development of \$94 million or 9 combined ratio points.

The underwriting results of Northbridge in 2018 included \$19 million of current period catastrophe losses, principally related to storms in Ontario and Quebec. And in Canadian dollar terms, Northbridge's net premiums written increased by 10% in 2018, reflecting strong retention of renewal business and price increases across the Group.

Moving to Odyssey. In 2018, Odyssey Group's underwriting profit increased to a \$181 million at a 93% combined ratio from an underwriting profit of \$60 million at a 97% combined ratio in 2017. Higher underwriting profit in 2018 principally reflected lower current period catastrophe losses and higher net favorable reserve development.

Current period catastrophe losses of \$252 million represented 9 combined ratio points in 2018, principally the events that I mentioned at the outset and other attritional current period catastrophe losses. And this was lower than the current period catastrophe losses of \$392 million, which represented 17 combined ratio points for Odyssey in 2017, principally related to Hurricanes Harvey, Irma and Maria.

Odyssey's combined ratio in 2018 also benefited from higher net favorable prior year reserve development of \$346 million or 13 combined ratio points. That development principally related to casualty and assumed property catastrophe loss reserves. Odyssey Group wrote \$2.9 billion of net premiums in 2018 which represented an increase of 16% from the prior year. This growth was spread across all of its divisions.

Crum & Forster. Crum & Forster's underwriting profit in 2018 increased to \$33 million at a 90% combined ratio from an underwriting profit of \$3 million and a combined ratio just slightly below 100% in 2017. The increase in the underwriting profit was principally due to higher business volumes and more profitable lines of business and lower current period catastrophe losses, partially offset by a modest decrease in net favorable prior year

reserve development. Crum & Forster's net premiums written increased by 6% in 2018, primarily reflecting growth in accident and health, umbrella, commercial multi-peril combined with the impact of rate increases.

Zenith National. Zenith National's underwriting profit in 2018 increased to \$140 million at an 83% combined ratio compared to underwriting profit of a \$117 million at an 86% combined ratio in 2017. The increase in the underwriting profit in 2018 principally reflected higher net favorable prior year reserve development and an improvement in the estimated accident year loss ratio. Net premiums written by Zenith in 2018 of \$789 million decreased by 6% year-over-year, principally reflecting price.

Brit. In 2018, Brit reported an underwriting loss of \$77 million and a combined ratio of 105% compared to an underwriting loss of \$202 million and a combined ratio of 113% in 2017. Current period catastrophe losses of \$210 million, representing 13 combined ratio points in 2018, principally related to the main catastrophe events mentioned at the outset. That was lower than current period catastrophe losses of \$259 million or 17 combined ratio points in 2017 that related principally to HIM.

Net favorable prior year reserve development was higher in 2018 at \$99 million compared to \$10 million in 2017. And Brit's net premium written increased by 9% in 2018 excluding the onetime intercompany reinsurance transaction with Runoff that is eliminated upon consolidation. The increase reflected the contribution from initiatives that Brit has launched in recent years, price increases and that's partially offset by reductions in non-core lines of business through active portfolio management.

Allied World. Allied World reported an underwriting profit of \$43 million and a combined ratio of 98% in 2018 compared to an underwriting loss of \$587 million and a combined ratio of 157% during the period Fairfax owned Allied in 2017. The improvement in underwriting profitability principally reflected lower current period catastrophe losses in 2018, which were \$223 million or 10 combined ratio points. And Allied World's underwriting profit in 2018 also benefited from \$97 million or 4 combined ratio points of net favorable prior year reserve development, which included better than expected emergence on the 2017 catastrophe losses, a reduction in unallocated loss expense reserve, partially offset by net adverse development in its casualty and professional liability lines of business. Allied World contributed \$2.4 billion in net premiums written in 2018, compared to 200 -- compared to 2017, which where Allied contributed \$992 million for the period at Fairfax owned Allied since its acquisition in July.

Fairfax Asia. Fairfax Asia's underwriting profit decreased to \$400,000 at a combined ratio of just below 100% in 2018 compared to an underwriting profit of \$38 million at a combined ratio of 88% in 2017 with the lower underwriting profit reflecting the absence in 2018 of the underwriting profit that was contributed by First Capital, which was sold in the fourth quarter of 2017 .

The insurance and reinsurance other segment reported an underwriting loss of \$49 million and a combined ratio of 105% in 2018 compared to an underwriting loss of 81 million and a combined ratio of 110% last year. The decrease in underwriting loss in 2018 principally

reflected lower current period catastrophe losses, which impacted the combined ratio by 2 points in 2018 compared to 10 points in 2017.

Moving to Runoff. Runoff reported an operating loss of \$198 million in 2018 compared to an operating loss of \$185 million in 2017. The increase in the operating loss in 2018 principally reflected higher net adverse development primarily related to asbestos and other loss reserves and increases in reserves for unallocated loss adjustment expenses. Partially offsetting this was an underwriting gain of \$85 million on the Part VII transfer and reinsurance transaction with the U.K. insurer that was disclosed in our third quarter 2018 interim report in the Runoff section.

Turning to some of the consolidated results. Consolidated interest and dividend income increased year-over-year from \$559 million in 2017 to \$784 million in 2018, primarily reflecting higher interest earned on increased holdings of short-dated U.S. treasury bonds and high quality corporate bonds. So it's partially offset by lower interest earned on U.S. state and municipal bonds as a result of sales during 2017 and 2018.

Fairfax recorded a provision for income taxes of \$44 million at a 5% effective tax rate in 2018. The lower effective tax rate in 2018 primarily reflected the gain on the deconsolidation of Quess which was not taxable.

Our total debt to total capital ratio increased to 27.2% at December 31, 2018 from 25.8% at December 31, 2017, and that was primarily a result of the decrease in our total capital. We ended 2018 with an investment portfolio which included holding company cash and investments of \$38.8 billion to slightly lower than \$39.3 billion that we held at December 31, 2017.

With that, I'll pass it back to you, Paul.

Paul Rivett {BIO 15243791 <GO>}

Thank you, Dave. We now look forward to answering your questions. Please give us your name, your company name and try to limit your questions to only one, so that is fair to all on the call. Okay, Angelica, we're ready for your questions.

Questions And Answers

Operator

Thank you. Our first question from Junior Ross, Private Investor. Your line is open.

Q - Junior Ross

Good morning, Paul.

A - Paul Rivett {BIO 15243791 <GO>}

Hi, good morning, Junior.

Q - Junior Ross

Two questions for you. The first question is the capitalization of investments, are we look at the private investments or the public investment? The second question would be, are we trying -- are we going to do aggressive buybacks this year, or is it going to follow the same fashion that we followed last year?

A - Paul Rivett {BIO 15243791 <GO>}

Junior, thanks for those questions. So the first one, first, we're looking to capitalize both private and public. So we're evaluating the entire equity portfolio and re-rating it to make sure it's our hurdle. And we're in the process as we speak of monetizing some of the private investments and we'll look at the public investments as well. So we're always looking to optimize. And this year, we're acutely focused on getting to that 15% return on equity target. And so, we will be monetizing equities.

On the buyback, we're very focused on as Prem said and I'm sure he'll talk about it at the annual meeting. Over the next 10 years, buying back substantially our stock. We've started doing that, as we mentioned, 340,000 shares in the last six weeks alone and we'll continue to do that. But always -- Junior always being prudent and keeping that holding company cash and marketable securities for a rainy day for safety. So, but I'll -- with that in mind, keeping being safe. We will use excess cash to buyback our shares particularly at these levels.

Q - Junior Ross

Okay, thanks.

A - Paul Rivett {BIO 15243791 <GO>}

Angelica, next question please.

Operator

Our next question is from Paul Holden, CIBC. Your line is open.

Q - Paul Holden {BIO 6328596 <GO>}

Yeah. thank you. Good Morning.

A - Paul Rivett {BIO 15243791 <GO>}

Good morning, Paul.

Q - Paul Holden {BIO 6328596 <GO>}

A question related to that 15% ROE target. You've done a lot to improve the operating income. I would argue that one of the levers you probably have left is on the underwriting

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average, not writing lot of premiums relative to equity, so maybe you can speak around thoughts and capacity there.

A - Paul Rivett {BIO 15243791 <GO>}

Yeah. So we have -- we'd certainly have capacity to grow. And we're in the right market. We will grow substantially. In the past, Odyssey's doubled its premiums. That --we're not seeing anything like that yet, Paul, but we are ready. And we think that particularly in the second half of the year, we could see increasing hardening. So to the extent that happens, we would love for our insurance companies to continue to grow. But that's what they have. We went through the stats and for the most part, other than Zenith where they're seeing some softening and that's what they do. They're really good at dialing it back when they see some softening in their market. They've reduced premium, but everybody else is growing and they will grow much more. We're sure that if there was a hardening.

Q - Paul Holden {BIO 6328596 <GO>}

Got it. Maybe you can just give us the organic premium growth for the quarter, if you have that number.

A - Paul Rivett {BIO 15243791 <GO>}

Yeah, let me just grab that, it's actually about the same as the year about 8.5%.

Q - Paul Holden {BIO 6328596 <GO>}

Okay, great. And then maybe one more question if I could. You haven't allocated more capital corporate bonds in a while, sounds like you did that in Q4. Just want to get a better understanding of that, is that because corporate spreads simply blow in the quarter and you thought it was a good opportunity to take advantage of that? Or has your thought around corporate credit changed on a go-forward basis?

A - Paul Rivett {BIO 15243791 <GO>}

No, our thoughts in corporate credit haven't changed. You're absolutely right, Paul. Spreads did widen out, particularly the short end. And we've stayed at the very short-end, so it's roughly equivalent to cash, but getting us that yield now, with that run rate of \$800 million of interest and dividend income. So we took advantage of opportunistically in the end of the last quarter of the year. And that's what we're best at. We will take advantage when it comes. But for now, we are very focused on staying at the short-end of the curve.

Q - Paul Holden {BIO 6328596 <GO>}

That's great. Thank you.

Operator

Next question from Jeff Fenwick, Cormark Securities. Your line is open.

Q - Jeff Fenwick {BIO 15350794 <GO>}

Hi, there, good morning, everyone.

A - Paul Rivett {BIO 15243791 <GO>}

Good morning.

Q - Jeff Fenwick {BIO 15350794 <GO>}

Paul, just a follow-up on the equity position monetization efforts that you got going on there. How should we think about that in terms of your view of just relative weighting of equities within the portfolio there? I mean are you talking about taking that weighting lower, or is this just a bit of a repositioning we're talking about?

A - Paul Rivett {BIO 15243791 <GO>}

I think it's just more of a recall or repositioning optimizing is what we're focused on, Jeff. So there's some things just that makes sense, given the price we think we can get for them to move them out. And others that just came in, like Toys "R" Us just came in, and there is some work that they need to do to optimize their operations. But for us, we're looking at selling things that will go at a good price. And right now, private equity is a focus in the marketplace. Number of people want those assets, and so we'll look to sell into that.

Q - Jeff Fenwick {BIO 15350794 <GO>}

I mean, I guess, one follow on, the other one obviously very large position now at Seaspan. I mean, can you just clarify for us, is there anything in that agreement about holding that position or being able to sell it down at any period of time in the near future? Or how should we think about how you're going to manage that going forward?

A - Paul Rivett {BIO 15243791 <GO>}

Yeah, so that, as you know, we really like David Sokol, and he is one of the best managers we think we've ever seen. And he's got Bing Chen as CEO, but David is intimately involved. And we think that's a good long-term hold. Obviously, everybody is focused on short-term and trade with China, but long-term having that kind of a business with David Sokol at the top, we think is something that can do very well. He has already been out there buying assets on the cheap and building up that business. And so for us, yes, so to answer your question, there's no need for us to hold. I mean it's available for sale, but this is when we think we could hold for a very long time. It's got a lot of runway with David and we could see great things from it. So we think it's one that's going to make us a lot of money over the long term.

Q - Jeff Fenwick {BIO 15350794 <GO>}

Okay. Thank you very much.

Operator

Next question is from Jaeme Gloyn, National Bank Financial. Your line is open.

Q - Jaeme Gloyn {BIO 19737597 <GO>}

Yeah, thank you. Good morning.

A - Paul Rivett {BIO 15243791 <GO>}

Good morning.

Q - Jaeme Gloyn {BIO 19737597 <GO>}

In the news last week or a couple of weeks ago, Fairfax rumored for to be looking at Protective Insurance. Not looking necessarily for you to comment on that rumor. But just in terms of M&A transactions in the insurance and reinsurance space, is there still an appetite to go down that path? Is there anything in particular that you would like to add or brief up, maybe some commentary around M&A in that space?

A - Paul Rivett {BIO 15243791 <GO>}

Yeah. So for us, that's a great question. We do get quite a lot. After we completed the acquisition of Allied World, we really do feel like we've done a big acquisitions we need to do. And to the prior question, we really think the thing to be focused on now is buying back our own stock. But that said, we do see specialty businesses more tuck-in things that we're looking at from time to time and we'll continue to do those. They are brought to us sometimes from our own companies. We've got, as you know, a fairly good reputation of treating entrepreneurs, owner very well and they want to bring their businesses to us. And if they make sense, we'll look at them, but they're more tuck-in type acquisitions.

On Protective, typically we don't talk about acquisitions until we've actually completed them, but that's one that, I would say, that we did receive the call and we -- just to say, because there is rumors about us being there that we are in fact not there and we will not be there. We're not interested. And we typically don't comment, but that's one just because our name is out there as being associated with it. Just to make it clear, we are not looking at Protective in anyway.

Q - Jaeme Gloyn {BIO 19737597 <GO>}

Okay. And then, maybe a little bit more granular question around the corporate and overhead. Is there anything that happened in the quarter that drove a little bit higher corporate overhead expenses that would be maybe one-time or something that you can point to?

A - Paul Rivett {BIO 15243791 <GO>}

There will be -- thanks for the question. There will be some more details on that in our interim report. There was a little bit of -- there was a reclassification in one of our operating companies of about \$11 million of underwriting expenses that really weren't underwriting expenses. They were more related to a startup operation. So I think you might be seeing that in the fourth quarter corporate overhead.

Q - Jaeme Gloyn {BIO 19737597 <GO>}

Okay, thanks. I'll turn it over.

A - Paul Rivett {BIO 15243791 <GO>}

Thank you. Angelica?

Operator

Next question from Tom MacKinnon, BMO Capital. Your line is open.

Q - Tom MacKinnon {BIO 2430137 <GO>}

Yeah, thanks very much. Good morning.

A - Paul Rivett {BIO 15243791 <GO>}

Good morning, Tom.

Q - Tom MacKinnon {BIO 2430137 <GO>}

With respect to the investment portfolio. It sounds like you're not changing your concentration or proportion of assets that you have in equities, just perhaps some more buying and selling in the portfolio kind of a reshuffling of holdings. Do I have this characterization of your monetization correct here?

A - Paul Rivett {BIO 15243791 <GO>}

Yeah, that's right, Tom. I mean, we think the team Wade and Lawrence and Prem and Roger that the team is salivating a little bit. It's a stock pickers market. There's things that we can invest in around the world. But you're absolutely right. We're looking primarily to optimize, it's not going to be a change in the mix.

Q - Tom MacKinnon {BIO 2430137 <GO>}

Okay. And -- or no change in the percentage of your portfolio that's in equities.

A - Paul Rivett {BIO 15243791 <GO>}

No.

Q - Tom MacKinnon {BIO 2430137 <GO>}

Okay. And then, with respect to the cash deployment, down considerably year-over-year and quarter-over-quarter, is there a kind of a magical percentage of your portfolio that you'd like to be in cash. And if you're just deploying it in the short-term stuff that seems just to be very temporary, where would you like to put it? Where would you like to deploy this money in the long run to try to hit your hurdle, because this is being so much in cash isn't helping, because it doesn't sound like given the concentration, given your -- what you

said about equity that you don't want to increase the equity position substantially, so where do you want to put this money?

A - Paul Rivett {BIO 15243791 <GO>}

So I mean, longer term, Tom, we'd like to go into longer-term fixed income, but we won't do it at the expense of quality or tenant, right. So we're thinking that over the near to mid-term here that the rates will rise and we just don't want to take any risk. So we're staying short end of the curve, but we're finding yield there. And where -- I said we're at about \$800 million of interest and dividend income run rate. We think maybe a \$1 billion achievable may be in that range on a run rate basis, but we will not reach for yield. And so, we're just sticking conservatively at the short-end of the curve.

Q - Tom MacKinnon {BIO 2430137 <GO>}

Okay, thanks for that.

Operator

Next question is from Daniel Chan, Private Investor. Your line is open.

Q - Daniel Chan {BIO 16137349 <GO>}

Good afternoon from Sweden.

A - Paul Rivett {BIO 15243791 <GO>}

Hi, good afternoon, good morning.

Q - Daniel Chan {BIO 16137349 <GO>}

Hi. I was wondering regarding the share buybacks from fourth quarter, so that you repurchased 150,000 shares at a cost of \$20.4 million, and that seems to be around \$135 per share, which sounds very cheap. Is that correct?

A - Paul Rivett {BIO 15243791 <GO>}

No, I don't think so. Dave?

A - Dave Bonham {BIO 15243784 <GO>}

Yeah, the share buyback in the fourth quarter was 52,000 shares at a cost of \$22 million and that's about \$434 per share. And then, we also did some buybacks for treasury about 98,000 shares at a cost of \$44 million, that's about \$451 per share. So our buybacks are coming in between \$430 and \$450 per share in the fourth quarter.

Q - Daniel Chan {BIO 16137349 <GO>}

Thanks. I also have another question, if I may.

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A - Paul Rivett {BIO 15243791 <GO>}

Absolutely.

Q - Daniel Chan {BIO 16137349 <GO>}

You are also writing that there were some amortization of some \$109.3 million regarding the subsidiary holdings intangible assets. Would you possibly provide some light regarding those write-offs or amortization?

A - Paul Rivett {BIO 15243791 <GO>}

So that amortization related to intangible asset amortization. So when we make an acquisition, part of the access that we pay over the fair value what or the carrying value what we acquire is either goodwill or intangible assets and a lot of what you're seeing there is amortization of customer relationships, broker relationships things like that, that were made in prior acquisitions relating to Zenith and Allied, especially Allied. More recently, that's kind of the big change period-over-period.

A - Dave Bonham {BIO 15243784 <GO>}

All right. But they're all according to plan I'd say.

A - Paul Rivett {BIO 15243791 <GO>}

Yeah, there is no impairments or anything in there, it's just normal course amortization. and I would just highlight on the corporate overhead. The other factor there that is -- that has made it increase in the quarter is just lower share of profit of associates. So we had some profit of associate related to Eurolife last year, and it wasn't as high this year. So that's the other factor.

Q - Daniel Chan {BIO 16137349 <GO>}

Got it. Thanks a lot.

A - Paul Rivett {BIO 15243791 <GO>}

Thanks, Daniel. Angelica, next question please.

Operator

Next question from Mark Dwelle, RBC Capital Markets. Your line is open.

Q - Mark Dwelle {BIO 4211726 <GO>}

Yeah, good morning. A couple of questions. First, related to the Runoff unit. I mean, I see the loss in the quarter was around \$96 million. I know you had the gain related to the transaction that you did, so was there a substantial reserve addition or something else in the quarter that kind of accounts -- squares those differences?

A - Paul Rivett {BIO 15243791 <GO>}

Yeah, we had some adverse development that I mentioned in my comments there, \$200 million or so, and that was on asbestos, other reserves, unallocated loss adjustment expenses and there was a little bit of an offset in there for some favorable development on workers' compensation business.

Q - Mark Dwelle {BIO 4211726 <GO>}

And that was all in the quarter, not for the full year?

A - Paul Rivett {BIO 15243791 <GO>}

That was mostly in the quarter. That's right.

Q - Mark Dwelle {BIO 4211726 <GO>}

Okay. The second question I had, within Brit, there was a fairly substantial decline in the net written premiums. You also mentioned there that there was an intercompany transaction. Could you just square how large that was, so that I can kind of get what the kind of the underlying run rate on the business was in the quarter?

A - Dave Bonham {BIO 15243784 <GO>}

Yeah. So the intercompany transaction that I referred to there was a reinsurance into Advent and the amount of the ceded premium or the amount that was affected, the net written premium was about a \$174 million. So that's the adjustment you make to Brit to get to the 9% growth rate that we set that Paul and I had mentioned in our comments.

Q - Mark Dwelle {BIO 4211726 <GO>}

Got it, thank you. And then the last question that I had related to, I guess, it primarily relates to the California fires. We've been seeing this stuff about the PG&E bankruptcy and the considerable insurance liabilities that they've incurred. Just Fairfax have any particular exposure to that?

A - Paul Rivett {BIO 15243791 <GO>}

We have just a little bit approximately \$25 million, Mark.

Q - Mark Dwelle {BIO 4211726 <GO>}

That's helpful. Thank you. Those are all my questions.

A - Paul Rivett {BIO 15243791 <GO>}

Thank you. Angelica, next question please?

Operator

Next question from Howard Slinker, Slinker & Company. You're line is open.

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Q - Howard Slinker

Thank you. Maybe I didn't hear you clearly. Could you please explain why Brit became so much after you bought it from Apollo?

A - Paul Rivett {BIO 15243791 <GO>}

Well, I don't think -- Howard, I don't think it actually decayed that much. I mean it's -- they've been hit more than our other companies with the catastrophe losses. I think is the primary thing that's happened to them, but Dave, I don't know if you want to add to that.

A - Dave Bonham {BIO 15243784 <GO>}

Yeah, I think that's fair enough. And if you're looking at the net premium written, as we talked about in 2018, it needs to be adjusted a little bit for that reinsurance transaction.

Q - Howard Slinker

But even if you take out the cat losses, the return on total capital would still be single digits, which is not what you believed, at least according to the prospectus of the deal when you bought Brit. So what's the difference?

A - Paul Rivett {BIO 15243791 <GO>}

No, I think, Howard it's primarily catastrophes. I mean, the Lloyd's market has gotten tougher. And so, there is a rebalancing happening in Lloyd's, we think over the long term, Brit's one of the companies that's going to benefit from that. But the other thing quite frankly as we've underperformed on investments, Howard. So we need to do better on that. But Brit with the team led by Matthew is doing very well and they will take advantage of what's happening in the Lloyd's market. So and -- but we need to do better on investments for them.

Q - Howard Slinker

Well, I'm curious, because what else would you say, but doing very well. When I looked at the transaction, I came up with different numbers than you came up with, and maybe their management is not as sharp as you originally estimated.

A - Paul Rivett {BIO 15243791 <GO>}

No, they're quite good, but we are happy to talk about it with you more Howard at any time.

Q - Howard Slinker

Sure. Okay, thanks guys.

A - Paul Rivett {BIO 15243791 <GO>}

Okay. Well, thank you.

Q - Howard Slinker

You're welcome.

Operator

Next question from Jeff Fenwick, Cormark Securities. Your line is open.

Q - Jeff Fenwick {BIO 15350794 <GO>}

Actually, sorry, my question was asked and answered. Thanks.

A - Paul Rivett {BIO 15243791 <GO>}

All right. Thanks Jeff. Angelica, next question please?

Operator

From Jaeme Gloyn, National Bank Financial. Your line is open.

Q - Jaeme Gloyn {BIO 19737597 <GO>}

Yeah, just wanted to quickly follow-up on the favorable reserve development in this quarter. Is -- was there anything in particular that was driving that, whether it's from the catastrophe losses from 2017? Is it a -- is it something that we can potentially read into maybe you're a little more conservative around catastrophe losses and this is something that can repeat in future years? And then a quick comment around the 2018 reserve development just being higher than your sort of longer run average run rate.

A - Paul Rivett {BIO 15243791 <GO>}

Yeah, so I can hit the first one. We saw about \$200 million of reserve redundancies from the cats from 2017. So that's one. Generally speaking, we have been very good over the last 10 years at conservatively reserving and have had reserve redundancies for the last 10 years. But with respect to the catastrophes in '17, that's led to about \$200 million of release. All right. Any other questions?

Operator

Your next question from Andrew Hollingworth, Holland Advisors. Your line is open.

A - Paul Rivett {BIO 15243791 <GO>}

Hello, Andrew.

Q - Andrew Hollingworth {BIO 1896571 <GO>}

Hi, good afternoon, Paul. How are you?

A - Paul Rivett {BIO 15243791 <GO>}

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Very good, thanks.

Q - Andrew Hollingworth {BIO 1896571 <GO>}

Great. Just one question from me. On the assets out of the balance sheet, when you talked after the question earlier on, you talked about the amount that's in equities and the amount that was in bonds and cash. While it's not prescribed, is that sort of break down something that you choosing to do in the very long-term to sort of match the liability side of the balance sheet?

And the reason I ask is, obviously, maybe a little bit more value was offered in terms of short-term corporate bonds in the fourth quarter, but mentioned quite a lot of value was on offering longer term assets, like sort of high-quality equities and you obviously didn't deploy in today. So just help me understand whether it's sort of the balance sheet structure we've got on the asset side is something that's slightly prescribed from the liability choice that you're making.

A - Paul Rivett {BIO 15243791 <GO>}

No, that was the choice we are making with respect to the equities that we held. I mean, roughly speaking, we're going to be somewhere in the neighborhood of 25% to 30% in equities generally and we added to the equities that we have. As I mentioned, we're adding now to Seaspan. You might have seen, we did a transaction with Grivalia and Eurobank that we think will do very well. But we're roughly in the zone where we want to be with respect to equities.

Q - Andrew Hollingworth {BIO 1896571 <GO>}

Okay. And if you wanted have a bigger percentage, you could. It's a choice you've made in terms of the asset blend you want to have in the business?

A - Paul Rivett {BIO 15243791 <GO>}

We're roughly at the upper end of our limit with respect to exposure, given the rules and regulations and that each of the regulators have in the insurance and reinsurance companies that we operate. So we're roughly at the top end of that range, Andrew.

Q - Andrew Hollingworth {BIO 1896571 <GO>}

Okay, great. Thank you for your help.

Operator

Next question from Mikel Abasolo, Solo Capital Management. Your line is open.

A - Paul Rivett {BIO 15243791 <GO>}

Good morning.

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Q - Mikel Abasolo {BIO 3756596 <GO>}

Yes, hello, good morning. Thank you for taking my question, Paul. And if I may, with my question I would like to challenge a little your equity portfolio positioning and the fact that you're aiming to reposition the equity side and the equity position in the asset side. From what I see you have roughly \$10 billion in equities on the asset side against \$11.8 billion of shareholders' equity. So those two are related, it seems like as you just said, in the upper range of what is allowable from a regulatory perspective.

But my question is, and I know we've been shareholders of Fairfax for a long time, and I know what you've been through with hedging the equity portfolio in previous years. And -- but my worry is that perhaps you're going long equities and I'm not questioning your -- the Seaspan peak or that other peak. But in terms of asset allocation, aren't you too exposed to equities now, precisely now when there seems to be an alternative for your float in the U.S. short-term fixed income market.

And precisely now when it seems that equities over the long run, and if you look at the indices or the asset categories, the U.S. equities can only go down. And my worry here is that if U.S. equities go to fair value, that would be easily 50% down from where they're trading today and that would wipe out 50% of your equity capital. Wouldn't it be prudent precisely now to go back to where you were in 2013, 2014 hedge at least a portion of your equity portfolio.

A - Paul Rivett {BIO 15243791 <GO>}

Yeah, so -- I mean, that's a good question. And I think from our perspective, if you look at our results longer term, we've done well. These short-term things that you tend to be focused on, you saw what happened in the fourth quarter and you saw the rebound. It is we think a stock pickers market. But we've got value stocks that we don't think will go down as much as the broader market and we don't really want to do the type of hedging we've done in the past, but yet we're conservatively positioned with so much in cash and short-term fixed income.

So, yes, the worry out there, what you're saying and work contrarian a little bit, Mikel. So we do like the stocks we have and we do think that it is a stock pickers market and we do think that relative to our peers that are assets are conservatively positioned, because we have so much in cash and short-term fixed income and the equity is our value equities that we believe. And that we believe we will withstand these kind of -- this volatility in this period. And meanwhile, while we're sitting conservatively positioned, we do think there's a high potential for a trade deal that will extend the runway in the U.S. and could potentially lead to the markets moving up for some period of time.

Q - Mikel Abasolo {BIO 3756596 <GO>}

Yes. Paul, just to clarify. When you said your conservative position because of the cash and your short-term bonds that you have. I mean, but that needs to be that way for, because of the liabilities that you have in your insurance operation, right. So what I'm saying is, I'm not doing a mistake by dividing the balance sheet between -- on the asset side, I would have cash and short-term. On the liability side, I would have the liabilities of your insurance

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and reinsurance operations. And then another separation another classification of your balance sheet would be I take your equities against your shareholders equity on the liability side.

So I don't gain much confirm from the fact that that you have plenty of cash in short-term treasuries or corporate bonds, because that is the default choice, since you're on insurance operation, right. So the equity exposure, and by the way, I like your stock picks as well, because I like you guys as value investors. But my worry is that if the market goes down 50% and it stays there, where it's ought to be trading for a long time that your solvency would be at risk and the whole thing would be at risk. That's like a big question I have.

And I don't get from your answer a relief of that, because as I see, you have \$10 billion -- \$10.3 billion in equities, that -- and I'm sure that Seaspan will do great and I'm sure that Euro Bank will raise eventually and so on, but if the market goes down 50%, I don't see a way for those stock positions to really bifurcate or divert from the market to that extent, you see. That would hit your equity.

A - Paul Rivett {BIO 15243791 <GO>}

I understand what you are saying, Mikel. And I think this is something probably better dealt with at the Annual General Meeting and Prem will address it. You'll have the chance to speak with all of our professionals, Wade and Lawrence and Roger. And they'll talk about it there. But I think we don't match assets and liabilities. And for us, we start in the fourth quarter was a nice test. Our stocks didn't go down as much as many as did. We do think that we're positioned conservatively with those stocks. And if there is something catastrophic like a 50% down, there aren't too many companies like us that have \$114 billion in things like credit deflation floors.

So we are positioned with things that we have on our balance sheet that we think will give us some lift, if there is something catastrophic like that, but then the other side of it is that in this market that we're -- it's a stock pickers market. We're looking at things and we're trying to do debt and warrants, and debt and warrants deals that will give us protection that others aren't getting. And we're having management that wants us to do those deals, unlike Seaspan where we can get the protection, get the yield and still have equity upside. So we think we're being prudent. But I think your question is a good one. And I'm sure we will come up at the AGM and that's probably the best place to deal with it.

Q - Mikel Abasolo {BIO 3756596 <GO>}

Thank you. Sorry for taking so much time. Thank you very much.

A - Paul Rivett {BIO 15243791 <GO>}

No problem, it's a good question. Thank you.

Operator

Our last question from (inaudible). Your line is open.

A - Paul Rivett {BIO 15243791 <GO>}

Thank you. Hi, Susan.

Q - Unidentified Participant

Hi, how are you? So my question is related to one of the investments that you guys made last year into Toys "R" Us Canada, and where that's kind of shaking out? And are you guys going to put more money in?

A - Paul Rivett {BIO 15243791 <GO>}

Yeah, no, it's turned out to be better than we expected in some ways and tough in others. So we bought it and basically, we're able to buy it for real estate value and in turns out that as we've looked the real estate. In fact, the real estate was worth more than even our purchase price. So we got a business that was making over 10 years, \$100 million of EBITDA year after year after year, basically for free. And 5,000 employees in 80 locations across the country and the Number 1 toy seller.

And as you've seen, I mean, retail, particularly through the Christmas season wasn't the greatest. But the company continues to generate EBITDA and with the team that we've got in retail, we're going to do very well. But it's a classic value investment and that we were able to purchase with all kinds of downside protection, got the real estate basically on the cheap and then got the business for free. And that's the type of deal we will do every time we see it, so it's been a good one for us.

Q - Unidentified Participant

Okay. So you're going to continue with the stores then?

A - Paul Rivett {BIO 15243791 <GO>}

Yeah, absolutely. Absolutely continue with the stores.

Q - Unidentified Participant

Perfect. Thank you so much.

A - Paul Rivett {BIO 15243791 <GO>}

Thanks, Susan. All right, Angelica.

Operator

Thank you. Mr. Rivett, you may now proceed.

A - Paul Rivett {BIO 15243791 <GO>}

Well, if there's no further questions Angelica, thank you for joining us on this call. We look forward to seeing you all at our Annual General Meeting in Toronto on April 11. Thank you very much, everyone. Thanks a lot Angelica.

Operator

Thank you. That concludes today's conference. Thank you for joining. You may now disconnect.

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