Q4 2012 Earnings Call

Company Participants

- Dave Bonham, CFO
- Paul Rivett, VP Operations
- Prem Watsa, Chairman and CEO

Other Participants

- Howard Flinker, Analyst
- Mark Dwelle, Analyst
- Paul Holden, Analyst
- Shazad Okigh, Private Investor
- Tim Piechowski, Analyst
- Tom MacKinnon, Analyst

Presentation

Operator

Good morning. Welcome to Fairfax 's 2012 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)

For time's sake, we ask that you limit your question to one. Today's call is being recorded. If you have any objections you may disconnect at this time.

Your host for today's call is Prem Watsa, with opening remarks from Mr. Paul Rivett. Sir, you may begin.

Paul Rivett {BIO 15243791 <GO>}

Thank you, Kathryn. Good morning. Welcome to our call to discuss Fairfax's 2012 year-end 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 filed with Canadian securities regulators.

I now turn the call over to our Chairman and CEO, Prem Watsa.

Prem Watsa {BIO 1433188 <GO>}

Thank you, Paul. Good morning, ladies and gentlemen. Welcome to Fairfax 's year-end conference call. I plan to give you the highlights and then pass it on to Dave Bonham, our CFO, for additional financial results.

Our book value per share increased by about 6.5% in 2012, to $378.10 per share, from $364.55 a share at the end of December, 2011, after we adjust for the $10.00 per share dividend that we paid in the First Quarter of 2012. We returned to profitable underwriting in 2012, notwithstanding $261 million losses from Hurricane Sandy, and $410 million in total catastrophe losses -- the fourth worst year for catastrophe losses that we have experienced in our history. OdysseyRe, in spite of Hurricane Sandy, had outstanding results, as its combined ratio was the lowest in its history at 88.5%. Fairfax Asia continues to do very well. And Northbridge, Crum & Forster, and Zenith are recovering very well from the soft markets of the past, showing underwriting discipline with good reserving.

For you, our shareholders, the most important point to recognize is that in 2012 our insurance and reinsurance businesses continued to expand after being in a downturn for the four years prior to last year. In 2012, including the acquisitions we made, net premiums written at Fairfax grew by 9.2%. Excluding acquisitions, which are First Mercury and Pacific Berhad in Malaysia, net premiums written grew by 7.4%. At the subsidiary level, net premiums written in 2012 grew as follows -- Zenith, plus 20.4%; Crum & Forster, plus 16.4%; OdysseyRe, plus 15%; Fairfax Asia, plus 12.6%; and Northbridge, in Canadian dollars, was down 6%.

The continued Catastrophe launches in 2012 -- which, by the way, Sandy was one of the largest catastrophes experienced in the United States -- very low interest rates and the potential lack of future reserve redundancies means there is no place to hide for the industry. Combined ratios have to drop well below 100% for the industry to make single-digit returns on equity with these low interest rates.

In the Investment area, net investment gains of $643 million for the year 2012 consisted of the following -- please note page two of our press release -- net gains on equity and equity-related investments of $1.12 billion, consisting of $470 million realized and $649 million unrealized gains, were reduced by net unrealized losses of $1.01 billion on our equity hedges. So our equity hedges were a significant negative for Fairfax in 2012. Net bond gains of $728 million, and other net losses of $199 million, resulted in a net investment gain of $643 million in 2012 for Fairfax. In total, we realized $1.07 billion in gains in 2012, which was offset by $422 million in unrealized losses, for net gains of $643 million. All of this is shown in the table on page 2.

Like in 2011, we reduced our long US Treasury position significantly at a very large realized gain. Please note, in 2011 and 2012, we've had total realized gains from stocks and bonds of $1 billion in each year. We believe that the unrealized losses represent, to a large extent, only market fluctuations, and if history is any guide, should result in profits over time.

As of December 31, 2012, the Company held $1.17 billion of cash, short-term investments, and marketable securities at the Holding Company level. Our Company continues to be soundly financed, with little near-term debt maturities, as we extended the term of our debt at lower interest rates in 2012 and early 2013 to allow the repurchase of about $230 million of maturing, more expensive debt. Finally, we continue to be approximately fully hedged at about 100% in relationship to our equity and equity-related securities, which includes convertible bonds and convertible preferred stock.

We continue to be very concerned about the prospects for the financial markets, and the economies of North America and Western Europe, accentuated by potential weakness in China. There appears to be a big disconnect between the financial markets and the underlying economic fundamentals. On October 12, 2002, the Company completed the purchase of the run-off business of Brit Insurance Ltd. for $335.1 million, which was almost fully paid by the Company's run-off subsidiaries. At December 31, 2012, Brit Insurance had an investment portfolio of $1.2 billion. In October 2012 the purported class-action commenced in July 2011 against the Company and Others was dismissed with no payment and without the possibility of further appeal or amendment.

On December 10, 2012 the Company completed the sale of its interest in Cunningham Lindsey for cash proceeds of $270.6 million. Fairfax invested $34.4 million of the proceeds in shares of Cunningham Lindsey on closing, to continue to be a 9.1% minority shareholder. In October 2012, the Company's TIG run-off subsidiary, paid $200 million in full satisfaction to loan note issued by TIG in connection with its acquisition of General Fidelity in August 2010. On October 15, 2012, the Company completed an offering at par of CAD200 million, of 5.84% notes due 2022, for net proceeds of approximately $199 million. Early this year, on January 21, 2013, the Company completed an additional $250 million offering of its 5.84% notes, due 2022, for net proceeds of $258.1 million. These notes were appraised at $103.854 per $100 principal amount, for an effective yield of 5.326%.

So now I would like to turn it over to Dave, so he can give you some more information on the underlying financials. Dave?

Dave Bonham {BIO 15243784 <GO>}

Thank you, Prem.

First, I'll focus on Fairfax's consolidated results for the Fourth Quarter and the full year of 2012. Then I'll move on to talk a bit about the Operating Company results. And finally, we'll finish up with the consolidated financial position.

So to the consolidated results -- for the full year of 2012, Fairfax reported net earnings of $532 million. That compares to $45 million of net earnings in 2011. Fully diluted earnings per share in 2012 was $22.94 per share. And that compared to a fully diluted loss per share of only $0.31 per share in 2011. Increased net earnings, year over year, was principally as a result of a significant improvement of the underwriting profitability of the Company. And I can elaborate on that a bit more in a moment.

For the Fourth Quarter of 2012, Fairfax reported net earnings of $404 million, or $18.90 per share on a fully diluted basis. That compares to the Fourth Quarter of 2011, when we reported a net loss of $771 million, or $38.40 per share on a fully diluted basis. An increase in net gains on investments was the primary driver of a year-over-year improvement in our Fourth Quarter net earnings; and much of what Prem has highlighted relative to our Investment performance in the full year of 2012 was also applicable to our investment results in the Fourth Quarter.

Turning to the underwriting results of our insurance and reinsurance operations -- for the full year of 2012, Fairfax reported a combined ratio of 99.8%, and an underwriting profit of $12 million. And this was in sharp contrast to the combined ratio of 114.2%, and the underwriting loss of $754 million that we reported last year. Current-period Catastrophe losses in 2012 were just over $409 million, and added 7 points to our combined ratio. And that was largely related to Hurricane Sandy. That compares to just over $1 billion of Catastrophe losses incurred in 2011, primarily comprised of the Japanese earthquake and the Thailand floods. And that added 19 points to the combined ratio in that year.

In terms of reserve development, in the full year of 2012, we experienced $177 million of net favorable development to prior-year reserves, and that benefited our 2012 combined ratio by 3 points. In 2011, net favorable emergence on prior-year claims reserves was $89 million, and that was a 1.7 benefited the 2011 combined ratio. Our accident year combined ratio in the full year of 2012 was 102.8%. And that compares to 115.9% in 2011. Excluding current-period Catastrophe losses, our accident year combined ratio was 95.8%, representing a near 1 point improvement over the 2011 accident year combined ratio of 96.6%.

Now, turning to our Operating Company results -- we'll start with OdysseyRe. In the Fourth Quarter of 2012, OdysseyRe earned an underwriting profit of $34 million, despite the impact of Hurricane Sandy losses, which were about $175 million, net of reinstatement premiums. Odyssey's combined ratio of 94.4% in the Fourth Quarter of 2012 included 31 combined ratio points of catastrophe losses. For the full year of 2012, OdysseyRe earned an underwriting profit of $267 million, and reported a combined ratio of 88.5%, representing a significant improvement relative to the underwriting loss of $336 million and combined ratio of 116.7% in 2011. That underwriting loss included $735 million of catastrophe losses, net of reinstatement premiums.

OdysseyRe's accident year combined ratio was 95.1% for the full year of 2012. And excluding current year catastrophe losses, that accident year combined ratio was 82.7%. That compared to the accident year combined ratio of 119.3% in 2011. That ratio included 37 combined ratio points of current-period catastrophe losses, so excluding catastrophes, Odyssey's accident year combined ratio last year was 82.6%.

In the full year of 2012, OdysseyRe's calendar year combined ratio included the benefit of 6.6 points, or $152 million of net favorable development of prior year's reserves, principally related to favorable emergence on prior year's Catastrophe losses, and Casualty and Property losses in the US and Europe. Odyssey wrote $2.4 billion of net premiums in the full year of 2012, up from just under $2.1 billion in 2011. The increase reflected the impact of a significant new Property quota share contract that incepted in 2012. And also reflected increased writings of US Crop and Umbrella lines of business.

Moving on to Crum & Forster, Crum & Forster incurred underwriting losses of $87 million in the Fourth Quarter, and $113 million in the full year of 2012. Underwriting losses in 2012 were principally as a result of $21 million of Hurricane Sandy losses in the Fourth Quarter, and net adverse development to prior year's reserves, $49 million in the Fourth Quarter, $54 million for the full year of 2012. And that reserve development was principally at First Mercury. As a result, Crum & Forster's calendar year combined ratio was 109.3% in the full year of 2012, and that compared to 107.9% in 2011.

Excluding the reserve development we just mentioned, Crum & Forster's accident year combined ratio was 104.9% in the full year of 2012, compared to 104.2% in 2011. Net premiums written by Crum & Forster in the full year 2012 were slightly in excess of $1.25 billion, compared to $1.1 billion in 2011. Excluding the year-over-year increase in net premiums that resulted from the consolidation of First Mercury in 2011, net premiums increased 7.5%, principally reflecting increases in specialty and standard lines of business.

Zenith National reported combined ratios of 114% and 115.6% in the Fourth Quarter and full year of 2012. And that showed significant improvement over the combined ratios of 132% and 127% in the same respective periods in 2011. The year-over-year improvement in the Zenith combined ratio reflected the combination of a decreased expense ratio, as a result of higher net premiums earned in 2012, and nominal net favorable development to prior year's reserves in 2012; compared to net adverse development to prior year's reserves, which added 6.8 points and 4.9 points to the combined ratios in the Fourth Quarter and full year of 2011, respectively. Net premiums written by Zenith of $619 million during the full year of 2012 increased year-over-year by 18.2%, reflecting premium rate increases, strong renewal retention, and the ability to write new business.

Northbridge's combined ratio in the Fourth Quarter of 2012 was 113.7%. And that compared to 101.9% in the Fourth Quarter of 2011, with the year-over-year increase primarily the result of $24 million of catastrophe losses, inclusive of reinstatement premiums, and those were primarily related to Hurricane Sandy. That added 10 points to the combined ratio in the Fourth Quarter of 2012. The full-year combined ratio for Northbridge in 2012 was 105.7%, and that compared to 102.8% in 2011.

The accident year combined ratio for Northbridge in the full year of 2012 was 111.8%. That included 4 combined ratio points of catastrophe losses and an increase in large losses year over year. The accident year combined ratio in the full year of 2011 was 106.5%, and that included 2.6 combined ratio points of catastrophe losses. Net premiums written by Northbridge of $949 million in the full year of 2012 compared to approximately $1.1 billion in 2011, and decreased by 13.6% when measured in US dollars.

After adjusting for the transfer of the renewal rights to Northbridge's US property book of business to an affiliate of OdysseyRe in May, 2012, and adjusting for a non-recurring inter-company reinsurance transaction that occurred in 2011, Northbridge's net premium written for the full year of 2012 decreased by 7.2% when measured in Canadian dollars. And that reflected lower retentions of existing business, partially offset by some modest price improvements and increased levels of new business in certain segments. The adjustments that I just mentioned, or I just referred to, and their impact on Northbridge, are set out on page 48 of our condensed consolidated financial statements for the Fourth Quarter and full year of 2012 and 2011, which is available on our website.

Fairfax Asia has reported a combined ratio of 84.4% in the Fourth Quarter of 2012. That represents a modest improvement over the combined ratio of 89.2% in the Fourth Quarter of 2011. For the full year of 2012, the combined ratio in underwriting profit of Fairfax Asia was 87% and $30 million, respectively -- or an underwriting profit of $30 million, respectively. That compares to 83% and $34 million in 2011. Net premiums written by Fairfax Asia increased by 12.6% to $241 million in the full year of 2012, from $214 million in 2011, and that was principally as a result of increased writings of Property and Engineering lines of business.

The insurance and reinsurance Other division in the full year of 2012 produced a combined ratio of 104.3% and an underwriting loss of $22 million. That compared to a combined ratio of 140.9% and an underwriting loss of $207 million in 2011. The significant improvement in underwriting results there reflected lower catastrophe losses year over year, partially offset by decreased net favorable developments in prior year's reserves.

In run-off, Prem has highlighted many of the significant transactions that happened in run-off during year. I'll round that out by saying that run-off had another good year, and reported $191 million of pretax income in the full year of 2012, compared to $360 million in 2011. Our consolidated interest and dividend income decreased year over year to $409 million from $705 million in 2011. Our interest and dividend yield decreased to 1.63% for the year ended December 31, 2012. That compares to a yield of 3.16% for the year ended December 31, 2011.

Our average investment portfolio size increased during 2012, primarily as a result of the acquisition of Brit Insurance. The average portfolio size based on the full year of 2012 was $25.1 billion. And that compared to $24.4 billion at the end of 2011. We ended the year with an investment portfolio, which included Holding Company cash and investments, of $26.1 billion.

Moving to our financial position, Prem captured most of the highlights related to that. And I'll add that our year-end debt to capital ratio decreased to 25.5%, compared to 26.4% in 2011, with the improvement primarily due to increased shareholders' equity, that being the result of our 2012 net earnings, partially offset by common and preferred share dividends paid.

And before I pass it back to Prem, I would like to remind everyone that our annual general meeting will be held on Thursday, April 11, at 9.30 AM at Roy Thomson Hall. The details will be in the annual report on the last page, which will be published in March 8 in the evening.

So back to you, Prem.

Prem Watsa {BIO 1433188 <GO>}

Thank you, Dave.

And now, we're happy to answer your questions. Please give us your name, your company name, and try to limit your question to only one so that it's fair to everyone on the call.

Okay, Kathryn, we're ready for the questions.

Questions And Answers

Operator

(Operator Instructions)

Paul Holden, CIBC.

Q - Paul Holden {BIO 6328596 <GO>}

I just want to ask two questions, if I may. And the first one is related to the trend in cat losses. Historically, we've normally thought of cat losses as making up 4% to 5% of premiums earned. Five-year average now is 9.5%. And 7% in the most recent year. Should we assume it's 4% to 5% going forward? And if that's the case, is it simply because pricing has made up for the differential? Is pricing adequate now, is my question.

A - Prem Watsa {BIO 1433188 <GO>}

Are you thinking in terms of our total return, non-capital, or investment returns? Or what were you thinking about?

Q - Paul Holden {BIO 6328596 <GO>}

Sorry, I'm thinking about cat losses as a percentage of premiums earned. Is pricing sufficient now that cat losses going forward should only make up 4% to 5% of premiums earned?

A - Prem Watsa {BIO 1433188 <GO>}

Yes. So we look at that right now and those percentages go up and down, as you know. But we think, because of the recent catastrophe -- so you have had a string of catastrophes in 2011. And you have had Sandy. Which, if it works out to be $25 billion to $30 billion -- and we'll only find out later on if that's what the actual cost is, that would be the second-largest catastrophe in the United States in total dollar amounts. So what that means is catastrophe pricing remains at very high levels. And we find it attractive. And subject to our limits, we are writing as much as we can now through OdysseyRe, particularly. And worldwide -- this is across the world. But over time, those rates will come down, if we don't have enough catastrophes in the next few years, not enough hurricanes damage or earthquake damage, that the pricing will be insufficient. But right now, it's attractive.

Q - Paul Holden {BIO 6328596 <GO>}

Okay. Thank you. Then second question is related to your equity hedges. And specifically I want to hone in on your private investments, or your investments in affiliated companies, as you call it. I want to understand why you're hedging that position from an economic basis. Obviously there is a mismatch from an accounting basis because you don't mark to market those investment every quarter. But how do you think about it from a real economic standpoint in terms of how you're going to extract value from those private investments? And why you feel you need to hedge the value of those.

A - Prem Watsa {BIO 1433188 <GO>}

Yes. These private investments, quite a few of them are public. We might have 20% of the company. Then we have to -- if we have anything about 20% we have to equity account it. But the underlying stock price is very much prevalent. And so we just think, right now we continue to be worried about the effects of economic weakness worldwide. And so we think that this is a good time to be conservative, including our equity positions in our Associates. Because the underlying -- a lot of the underlying companies that sell public. We're basically very conservative at this stage.

Q - Paul Holden {BIO 6328596 <GO>}

Okay. Thank you.

Operator

Tom MacKinnon, BMO Capital.

Q - Tom MacKinnon {BIO 2430137 <GO>}

Just again to ask the question, I asked a similar question the last quarter, but you're getting underwriting improvement here, certainly from an accident year, excluding cats basis. But the drag from being 31% invested in cash continues to weigh on your operating results, if you will. What's it going to take for you, or what signals would you look for in the market before you'd want to reduce that cash position? Is there anything other than just you think you're going to wait and get a better return? Or what's driving you to continue to be 31% invested in cash?

A - Prem Watsa {BIO 1433188 <GO>}

That's a very good question, Tom. We've got about 30% cash, a significant amount of cash in the Company. First of all, as I said in our opening remarks, there's a disconnect from the financial markets -- and I mean stock and bond markets here -- versus the underlying fundamentals. What do I mean? Stock markets have gone up very significantly from the end of 2009. From the March of 2009, the bottom, gone up more than 100%. And the spreads between corporate bonds and treasuries are now comparable to what they were prior to 2008. And the economy, even last quarter, in the United States was flat or down 0.5%. So in spite of QE3, in spite of QE2, QE1, all of that massive stimulus, monetary stimulus, hasn't had much of an impact on the economy. And so we're just thinking that it's a time to be conservative.

We think what happened in '08, '09, was not like any other economic recession. Tom, we mentioned a few times, we think this is a 1 in 50, 1 in 100 year storm. So you have to be prepared for its after effects. We don't think it just lasted for three and six months and so now we can go forward. This is an opinion, by the way. And we could very much be wrong. And so, we just feel that way.

As far as the 30% cash, remember, that can change. So in 2008 -- and we had this position in 2007 and 2006 -- 2008 things turned, the financial markets. The stock markets dropped during that time about 50%. And so we took our hedge off. And spreads widened significantly. Like, really huge spreads. In turn, the only people who could benefit from that were the people who had cash or government bonds. And so we're conscious of that in our history. Cash gives you options, gives you the ability to take advantage of opportunity. But you have to be long term. We have built our Company with a long-term view. Our long-term results are excellent.

For example, in 2007, '08 and '09 -- the three years 2007, 2008, 2009 -- we made $2.8 billion after-tax. Our book value went up by 150%. Since that time, we haven't done a lot. But we've said to our shareholders that we are long-term focused, our results are lumpy, and we never know when it can change. But the cash gives us a huge advantage in terms of taking advantage of opportunity as and when they come. At the moment, we don't think there are many, so we're building cash.

I did say, one last point, that in 2011 and 2012, we've realized -- when I say realized, I mean we've sold stocks and bonds -- and realized $1 billion in each year. But it's masked by the mark-to-market accounting which takes the fluctuations and subtracts from that $1 billion. We think over time those things will work themselves out. So we really think we're in a very good position, but always with a long-term viewpoint, Tom.

Q - Paul Holden {BIO 6328596 <GO>}

Thank you for that.

Operator

Mark Dwelle, RBC Capital Markets.

Q - Mark Dwelle {BIO 4211726 <GO>}

A couple questions, both related to the run-off segment. You added a fairly significant deal late in the quarter, to do reinsurance for Eagle Star. Could you just give some background in terms of what type of underlying risks those are? The liability or property, whatever they might be?

A - Prem Watsa {BIO 1433188 <GO>}

Yes. Eagle Star, Tom, was another deal that we did late in the year. Our annual report comes out, Tom, on March 8. And we'll give you a lot more detail, not only, of course, on our run-off acquisitions, but also on our views on the financial markets. That's the opportunity to tell you a lot about some of these acquisitions. But one office has done an outstanding job for us. Eagle Star is one. And Brit, as you know, is the big one that we acquired in 2012. And it's after a significant amount of due diligence.

We've got a team, that's all they do is run-off. They're specialized in run-off. And so we just think that's a major advantage. There's very few companies that can do this. There's maybe two or three companies that compete with us. And we have our historical reputation of striking a deal and never changing it. Subject to due diligence, but never changing it. Unless we find something different -- and we haven't in 27 years. That is a huge advantage for us when we do these transactions. But more on Eagle Star in our -- Dave, did you want to add to that, perhaps?

A - Dave Bonham {BIO 15243784 <GO>}

Yes. Mark, just to your question, that Eagle Star portfolio is largely concentrated in the London market business. It's got some US casualty business and it's looking at older claims, 1990 and prior.

A - Prem Watsa {BIO 1433188 <GO>}

Yes. And Mark, very similar to the businesses that we've done in the past. So we've got lots of experience. Their Files are very similar to what we've been already administrating. So there's a huge advantage because many of these books are very similar. And we take 10% participation, or 15% participation, and Eagle Star might be taking comparable participations on similar accounts. So our people would have a big advantage in knowing the details on these files.

Q - Mark Dwelle {BIO 4211726 <GO>}

Okay. Thanks. It sounds like that's a pretty mature book of business. And certainly the run-off unit has done extremely well this year. The other question I had also related to the run-off. When you brought over Brit, closed early in October, there was a little bit of earned premium and associated loss reserves. Would there be much more of that? Or was that just the last, final closing gasp of that before it goes fully into run-off?

A - Prem Watsa {BIO 1433188 <GO>}

Yes, Dave, do you want to take that?

A - Dave Bonham {BIO 15243784 <GO>}

Sure, Mark. When we got that acquisition, there were a few policies that were still in force when we took it. So we took responsibility for those policies. So those policies are just going to run off, and that will peter out over the next nine months to 12 months and there shouldn't be any more premium coming in through there.

Q - Mark Dwelle {BIO 4211726 <GO>}

So it should taper down from $30 million -- $30 million was the earned in the Fourth Quarter -- so it should taper down from there to nothing over the next nine months, give or take?

A - Prem Watsa {BIO 1433188 <GO>}

Mark, on that transaction, one of the key risk factors, from our standpoint, was we identified reserves that we were not as comfortable with. And so we reinsured them to Brit, with the idea that we have an option, in 18 months, to commute those results and bring them back. As we get more familiar with the reserving practices, the reserving claim files, then we can bring them back. If we so desire. But that reinsurance transaction back to Brit was a very important component of our due diligence.

Q - Mark Dwelle {BIO 4211726 <GO>}

That's definitely brought a lot of assets to bear on the balance sheet. And if it's a successful investment, that should go a long way. So good luck with that one. Those our all my questions, thanks.

Operator

Howard Flinker, Flinker & Co.

Q - Howard Flinker

Is the difference between premiums written in the income statement --.

A - Prem Watsa {BIO 1433188 <GO>}

Just a little louder, Howard?

Q - Howard Flinker

Is the difference between net premiums written in the income statements, and in that short table, the run-off?

A - Dave Bonham {BIO 15243784 <GO>}

Can you just elaborate a bit more there, Howard?

Q - Howard Flinker

Yes. In that table where you have divisional premiums written, using the Fourth Quarter, the premiums written totaled 1399. And in the income statement, the premiums were 1598. I'm talking net premiums.

A - Prem Watsa {BIO 1433188 <GO>}

You wanted a reconciliation? Howard, why don't you give Dave a call a little later on and he'll reconcile that for you.

Q - Howard Flinker

Fair enough. That's my question.

Operator

Tim Piechowski, ACR.

Q - Tim Piechowski {BIO 16907769 <GO>}

At this point, the Company has outstanding CAD2.6 billion worth of preferreds and debentures. My question would be, given that Northbridge is continuing to decrease premiums written, how much of the CAD2.6 billion outstanding you think of as a hedge for Northbridge and other Canadian operations, versus a short position, given the Canadian dollar or (inaudible) economies generally?

A - Prem Watsa {BIO 1433188 <GO>}

Tim, what we basically do with the preferreds, particularly, we are hedging our capital, which is in excess of $1 billion in Canada. So we have Northbridge with capital -- Dave, what is Northbridge's capital?

A - Dave Bonham {BIO 15243784 <GO>}

Say, about $1.3 billion.

A - Prem Watsa {BIO 1433188 <GO>}

$1.3 billion. So we're hedging that $1.3 billion in Canadian dollars because we report in US dollars, Tim. And so, we're just using that as a hedge so it doesn't impact our financial statements. Dave, you want to add to that?

A - Dave Bonham {BIO 15243784 <GO>}

Yes. That's right. The amount of the Canadian dollar debt is more or less now matched to the net assets of Northbridge in Canadian dollars. So that's the principal component of the hedge.

Q - Tim Piechowski {BIO 16907769 <GO>}

Good. Thank you, Tim.

Operator

(Shazad Okigh), private investor.

Q - Shazad Okigh

A bit of an open-ended question here for you, maybe following on from Tom. This is obviously a time where corporate margins are at unseen levels, 70% or 80% above historic averages. We're still at a very high Shiller PE patio when you look at earnings over the last ten years. And as you mentioned earlier, lows in corporate bond yields, particularly junk yields. So margin of safety seems to be very low. But the question for you is, do you see this carrying on for -- could this potentially carry on for a very long time, given the Fed printing $1 trillion a year with their open-ended program and very large US deficits? So are we in a position where this situation could persist for a long time going forward?

A - Prem Watsa {BIO 1433188 <GO>}

Shazad, that's a very good question. And of course, no one knows the answer to that. But all of the factors that you mentioned are impacting the marketplace. We are going to discuss this more, Shazad, in the March 8 annual report. And we're also going to discuss it at our annual meeting. And you're really welcome to come in, ask the question, and we'll have a nice free discussion.

But really, when this will change, Shazad, really no one knows. Our view is that we have to be very strong financially, where we don't want to ever be indebted to the kindness of friends, or the Federal Reserve or the Bank of Canada. We have to be independent. We have to look after our capital so that under any circumstances we don't need capital. And so, we're very conscious of the downside. While at the same time looking for opportunity. And we're finding quite a bit. And we're realizing quite a bit of gains, as I had mentioned to you. So it's a fine balance and we watch that very carefully everyday.

Q - Shazad Okigh

Thanks.

A - Prem Watsa {BIO 1433188 <GO>}

Thank you, Shazad. Any other questions, Kathryn?

Operator

We have no further questions at this time.

A - Prem Watsa {BIO 1433188 <GO>}

So if there are no more questions, thank you all for joining us on this call. We look forward to presenting to you again after the 2013 First Quarter. We also look forward to seeing you at our annual meeting on April 11. Thank you.

Operator

This will conclude today's conference. All parties may disconnect at this time.