

Fairfax Financial Holdings Limited TSX:FFH

FY 2015 Earnings Call Transcripts

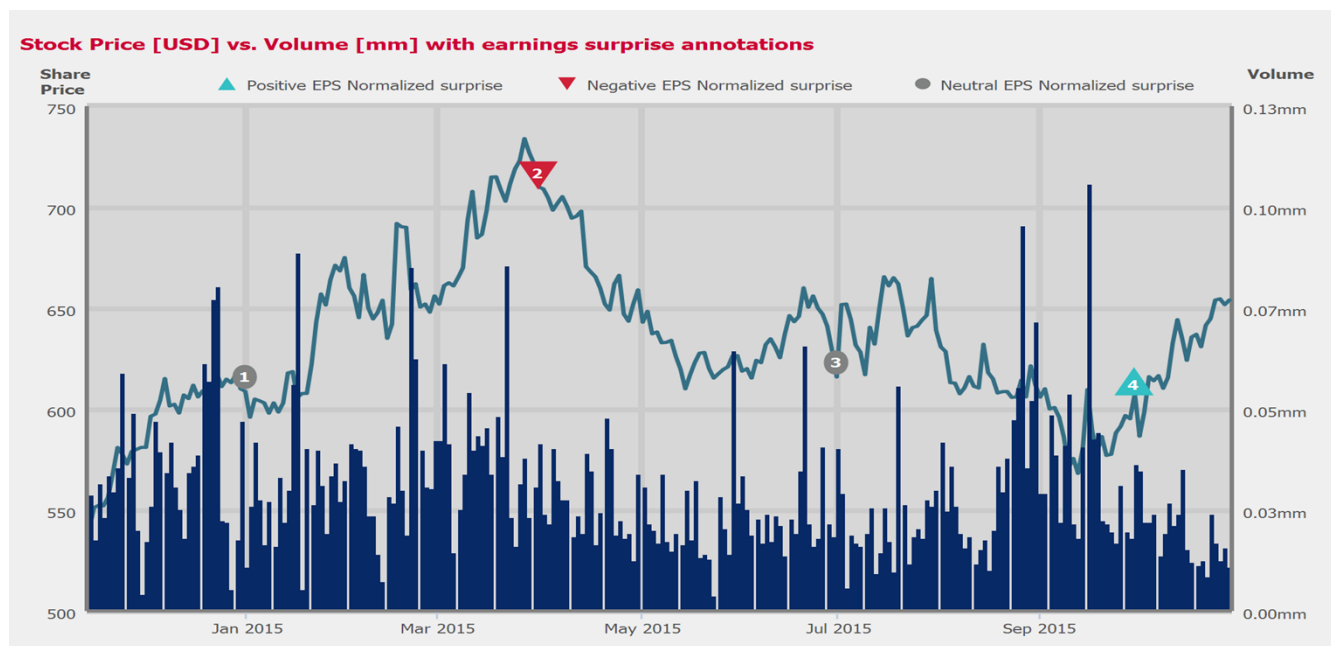
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S&P Capital IQ Estimates

	-FQ4 2015-			-FQ1 2016-		
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	SURPRISE	CONSENSUS
EPS Normalized	5.60	13.65	▲ 143.75	5.87	▼ (64.48 %)	19.62
Revenue (mm)	2705.70	2447.20	▼ (9.55 %)	2738.30	▲ 9.47	9872.60

Currency: USD

Consensus as of Jan-25-2016 12:23 PM GMT



Call Participants

EXECUTIVES

David J. Bonham

Chief Financial Officer and Vice President

Eric P. Salsberg

Vice President of Corporate Affairs and Corporate Secretary

V. Prem Watsa

Founder, Chairman and Chief Executive Officer

ANALYSTS

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Jeffrey Michael Fenwick

Cormark Securities Inc., Research Division

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ATTENDEES

Mikel Abasolo

Andrew Bell

Paul David Holden

CIBC World Markets Inc., Research Division

Ronald David Bobman

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Sean Barry

Tom MacKinnon

BMO Capital Markets Equity Research

SHAREHOLDERS

Presentation

Operator

Good morning, and welcome to Fairfax's 2015 Year-End Results Conference Call. [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 Prem Watsa with opening remarks from Rick Salsberg. Mr. Salsberg, you may begin.

Eric P. Salsberg

Vice President of Corporate Affairs and Corporate Secretary

Thank you. Good morning. Welcome to our call to discuss Fairfax's 2015 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, which has been filed with Canadian securities regulators and is available on SEDAR.

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

V. Prem Watsa

Founder, Chairman and Chief Executive Officer

Thank you, Rick. Good morning, ladies and gentlemen. Welcome to Fairfax's conference call on its 2015 results. I plan to give you some of the highlights and then pass it on to Dave Bonham, our CFO, for additional financial details.

Our underwriting results in 2015 were the best in our 30-year history with record underwriting profit of \$705 million and net earnings of \$568 million. We had a record low of combined ratio of 89.9% with OdysseyRe at 84.7% and all our major insurance companies having combined ratios less than 100%. We also had net investment losses of \$259 million in 2015 for the whole year, including realized gains of \$1.2 billion offset by unrealized losses of \$1.4 billion. We are maintaining our defensive equity hedges and deflation protection as we remain concerned about the financial markets and the economic outlook in this global deflationary environment.

Our insurance and reinsurance businesses premium volume increased in 2015 by approximately \$1 billion, primarily due to the acquisition of Brit, which had a combined ratio of 94.9% since we purchased it in June 5, 2015. The combined ratio for our insurance and reinsurance operations in 2015 was 86.4% for the fourth quarter and a record 89.9% for the whole year. As I said earlier, we made a record underwriting profit of \$705 million in 2015.

At the subsidiary level, the change in net premiums written in 2015 compared to 2014 and combined ratios were as follows: OdysseyRe had a 12.5% decrease in net premiums and a combined ratio of 84.7%. The decrease in premiums were mainly because of the exchange rate and the nonrenewal of a large Florida property cover; Crum & Forster had an increase of 23% and a combined ratio of 97.7%; Northbridge, in Canadian dollars, increased its premium, net written premiums by 6% and a combined ratio of about 91.8%; Zenith, up 9% and a combined ratio of about 82.5%; finally, Fairfax Asia had a 1.5% drop in premium and a combined ratio of 87.9%. Fairfax Asia was also affected by the foreign exchange rates.

Insurance and reinsurance operations produced operating income, excluding net gains and losses on investments, of \$1.2 billion compared to \$915 million in 2014, primarily as a result of improved underwriting profit and higher interest and dividend income.

As shown on Page 2 of our press release, we realized gains on our investment portfolio of \$1.2 billion during 2015. Excluding our hedging gains and before mark-to-market fluctuations in our investment portfolio, we earned \$1.9 billion in pretax income. Including all hedging gains and mark-to-market fluctuations in our investment portfolio, we reported pretax income of \$625 million and after tax income

of \$568 million in 2015. You will note that in 2015, our investment portfolios went up to \$28 billion from \$26.2 billion, mainly because of the acquisition of Brit Insurance.

In 2015, long U.S. government bond rates increased a little and our common stocks did better than the Russell 2000 index, which decreased 5.7%. We have yet to significantly benefit from our hedges and our approximate \$110 billion notional amount of deflation swaps, and of course, our cash position gives us great optionality. At our last Annual Meeting, we made the point that while we were protecting our capital on the downside, our investment portfolio could also do very well. Our common stock portfolios continued to be hedged at approximately 90%. Early in 2016, we increased the hedge to 100%.

On the investment side, net investment losses of \$259 million in 2015 consisted of the following: As shown on the table on Page 2 of our press release, we had net gains on equity and equity-related investments after the hedges of \$76.8 million, resulting from a \$501.8 million net gain in our equity hedges, because of the 5.7% decrease in the Russell index, offset by net losses of \$425 million in the equity and equity-related investments. These are all shown on Page 2 of our press release.

We realized gains of \$818.8 million in our equity and equity-related holdings in 2015. Also, at the end of 2015, we had unrealized losses of \$495 million in our bond portfolio because of a small rise in interest rates, as I mentioned to you. As we've said in our Annual Meetings, Annual Reports and Quarterly Reports, with IFRS accounting, where stocks and bonds are recorded at market and subject to mark-to-market gains and losses, quarterly and annual income will fluctuate widely and investment results will only make sense over the long term.

CPI inflation continues to be at or below 1% in the United States and Europe, levels that we have not seen since the 1950s. In fact, it may surprise many of you to know that in the second half of 2015, the U.S. had deflation of 0.9% at an annualized rate of 1.8% and Europe at 0.5% or an annual rate of 1%. That's deflation. That is to say prices went down in the second half of 2015 at an annualized rate of 1.8% in the United States and 1% in Europe. This is in spite of QE1, 2 and 3.

Long bond -- long-term government bond rates in Europe are making record lows, quite often the lowest in 200 years. In Germany, more than half the German government bond market is yielding negative interest rates. Also, 8 countries in Europe already experiencing deflation. 30-year long German bond rates are currently below 1%. In Japan, 10-year government bond rates are below 0%. That is negative yields. The spread between 30-year U.S. long rates and 30-year government bond rates is close to a record as German rates have fallen much faster than the United -- U.S. rates.

Although our CPI-linked derivatives with a notional value of approximately \$110 billion decreased in market value in the fourth quarter, with deflation in the air, these contracts have come to life in 2016, but they continue to be very volatile. The majority of the contracts are based on the U.S. CPI index, about 54%, or the European Union CPI index, about 40%. Further information is available on Page 3 of our press release where we've included a table on our deflation swaps. On average, they have 6.6 years to run. As I've said before to you, our CDS experience comes to mind. Also, I've emphasized in the past that it took 5 years -- 5 long years in Japan before deflation set in for the next 18 years.

When you review our statements, please note that we own more than 20% of a company via equity account and about 50% we consolidate so that mark-to-market gains in these -- companies are not reflected in our results. The fair value of our investments in associates is \$2.19 billion with a carrying value of \$1.73 billion and unrealized gain of about \$456 million. This is not on our balance sheet. Also, Thomas Cook was just consolidated, and our financial statement is doing very well compared to our original purchase price. We purchased Thomas Cook at INR 52 per share in 2012, and it's trading at close to INR 200.

We continue to be concerned about the prospects of the financial markets and the economies of North America and Western Europe, accentuated, as we've said many times before, by the potential weakness in China. Early in 2016, these concerns are being reflected in the marketplace with the Russell 2000 being down more than 10%. We see the potential for major dislocations in the marketplace with many significant unintended consequences, and we want to protect our company from them. As of December 2015, we have \$7.3 billion in cash and short-term investments, which is 26% of our total investment portfolio, to

take advantage of opportunities that may come our way. Also, our treasury and municipal bond portfolio of \$9.3 billion is very liquid.

On October 30, 2015, Fairfax agreed to acquire an additional 9% of the outstanding shares of ICICI Lombard. ICICI Lombard is the largest private sector general insurance company in India with gross written premiums of approximately \$1 billion for the year ended March 31, 2015. Upon completion of the transaction, the share ownership in ICICI Lombard of ICICI Bank will be -- and Fairfax will be approximately 64% for ICICI Bank and 35% for Fairfax. The proposed transaction values ICICI Lombard at \$2.6 billion, reflecting ICICI Lombard's position as a leading private sector general insurance company in India and the substantial potential for profitable growth of its business. Closing of this transaction is subject to government and regulatory approval.

On December 22, 2015, Fairfax agreed to acquire an 80% interest in Eurolife Insurance Group for a purchase price of \$347 million. Eurolife, which distributes its life and nonlife insurance products and services through Eurobank's network, is the third-largest insurer in Greece with gross written premiums of \$241 million for the 9 months ended 2015. The transaction is subject to regulatory approvals and closing conditions and expected to close by the end of the second quarter of 2016.

We continue to be soundly financed with year-end cash and marketable securities in the holding company of \$1.3 billion. The company's total debt to total capital ratio improved to 21.8% at December '15 compared to 24.6% at December 31, 2014.

Now I'd like to turn it over to Dave Bonham, our CFO, so we can give you some more information on the underlying finances. Dave?

David J. Bonham

Chief Financial Officer and Vice President

Thank you, Prem. To start off with, I wanted to let you know that in addition to the press release that we issued yesterday, all of the details of our fourth quarter and year-to-date financial results will be made available in our Annual Report, which will be posted to our website on March 11, 2016.

So now we'll move on to Fairfax's consolidated results for the full year of 2015, some details of the operating company results and then on to our consolidated financial position. For the full year of 2015, Fairfax reported net earnings of \$568 million or \$23 per fully diluted share, and that was lower than 2014 when we reported year-to-date net earnings of \$1.6 billion or \$73 per fully diluted share. The decrease in net earnings principally reflected net investment losses in 2015, whereas in 2014, we had significant net investment gains, and that was partially offset by increased underwriting profit.

Underwriting profit at our insurance and reinsurance operations increased to \$705 million in 2015 with a combined ratio of 89.9% compared to underwriting profit of \$552 million and a combined ratio of 90.8% in 2014. Year-over-year, underwriting profit was up by \$153 million. The consolidated combined ratio continued to benefit from net favorable reserve development and very modest cat losses, trends that have continued to run throughout 2015.

Net premiums written by our insurance and reinsurance operations increased by 17% in 2015, principally reflecting the consolidation of Brit's net premiums written of \$946 million.

So turning to our operating company results. We'll start with OdysseyRe. In 2015, OdysseyRe reported an underwriting profit of \$337 million at a combined ratio of 84.7%, and that compared to an underwriting profit of \$360 million and a combined ratio of 84.7% last year. Lower underwriting profit in 2015 principally resulted from a decrease in premiums earned with lower non-catastrophe underwriting margins, which included the impact of the Tianjin port explosion in China, which decreased underwriting profit by \$53 million or 2.4 combined ratio points. Underwriting profit in 2015 was also affected by lower writings of higher-margin catastrophe business, partially offset by lower current period catastrophe losses and increased net favorable prior year reserve development.

OdysseyRe wrote \$2.1 billion of net premiums in 2015, a decrease of about 12.5% over 2014. The decrease principally reflected the impact of a significant quota share reinsurance contract that did not

renew in 2015 following a decision by the cedent to retain all the risk associated with that contract. That resulted in the return of \$100 million of premium to the cedent in the second quarter of 2015. The decrease also reflected the impact of unfavorable foreign currency translation at OdysseyRe's EuroAsia division.

Now moving on to Crum & Forster. Crum & Forster's underwriting profit increased from \$3 million at a 99.8% combined ratio in 2014 to \$15 million at 97.7% in 2015. There is no net prior year reserve development in either 2015 or 2014, and current period catastrophe losses were modest in 2015 and comparable to the levels experienced last year. Crum & Forster's net premium written increased by 23% in 2015, primarily reflecting growth in Fairmont's accident and health business and across all lines of business at Crum & Forster and also included improvements in the pricing of casualty reinsurance purchased and reductions in purchases of quota share in facultative reinsurance, and this was partially offset by planned reductions in the legacy CoverX business.

Zenith. Zenith National reported increased underwriting profit in 2015 of \$134 million and a combined ratio of 83%, and that compared to underwriting profit of \$90 million and a combined ratio of 88% in 2014. The improvement in 2015 principally reflected a lower estimated current accident year loss ratio, earned price increases that were equal to estimated loss trends for the accident year 2015 and net favorable development of prior year reserves that was slightly higher in 2015. Net premiums written by Zenith was \$785 million, increased by 9% in 2015 and that principally reflected an increase in exposure.

Turning to Northbridge. Northbridge reported increased underwriting profit of \$71 million and a combined ratio of 92% in 2015 compared to an underwriting profit of \$43 million and a combined ratio of 96% in 2014. Northbridge's underwriting results in 2015 reflected improvements in its non-catastrophe loss experience related to the current accident year and the continuation in 2015 of the benefit from net favorable prior year reserve development but to a slightly lesser extent relative to 2014. There were no material current period catastrophe losses in 2015 or 2014. In Canadian dollar terms, net premiums written by Northbridge in 2015 increased by 6%, reflecting modest price increases across the group, increased renewal business and a decrease in the amount of casualty reinsurance purchased.

Fairfax Asia's underwriting profit of \$35 million and its combined ratio of 88% in 2015 was fairly consistent with its underwriting profit of \$36 million and combined ratio of 87% last year. Net premiums written by Fairfax Asia decreased by 1% in 2015, and that reflected planned reductions in commercial automobile writings at Falcon, the unfavorable effect of foreign currency translation at First Capital and Pacific Insurance and an increase in written premiums ceded to reinsurers related to a new intercompany quota share reinsurance agreement with Group Re that incepted at the start of this year. That was all partially offset by the positive contributions to net premiums written related to the acquisitions of Union Assurance, MCIS and Fairfax Indonesia.

The insurance and reinsurance other segment produced an underwriting profit of \$46 million and a combined ratio of 90% in 2015, an improvement relative to the underwriting profit of \$21 million and combined ratio of 95% in 2014. The increase in underwriting profit in 2015 principally reflected higher net premiums earned, lower current period catastrophe losses and increased net favorable prior year reserve development, and that was partially offset by a year-over-year reduction in non-catastrophe underwriting margins related to the current accident year.

Net premiums written by the insurance and reinsurance other segment increased by 18% in 2015. And that increase reflected growth in the accident health line of business at Advent and the positive impact of business assumed by Polish Re from QBE in Eastern Europe, and that was partially offset by lower writings of property business at Polish Re.

Turning to Brit. Fairfax completed the acquisition of Brit on June 5, 2015, and commenced consolidating Brit's financial reporting from that date. For the period June 5 or June 5, 2015, to December 31, 2015, Brit contributed \$946 million of net premiums to the consolidated total and produced an underwriting profit of \$45 million at a 94.9% combined ratio.

Turning to some of our consolidated results. Consolidated interest and dividend income increased from \$404 million in 2014 to \$512 million in 2015, reflecting interest income earned on increased holdings of

higher-yielding government bonds year-over-year and the consolidation of the investment portfolios of Fairfax India and Brit.

Fairfax recorded an income tax recovery of \$18 million in 2015 relative to pretax earnings of \$625 million, producing a negative effective income tax rate. The negative effective income tax rate principally reflected the impact of our regularly-recurring nontaxable investment income and also reflected the impact of a gain on sale of Ridley and also in connection with the Cara acquisition, which were either taxed at capital gains rates in Canada where only 50% of the gain is taxable or where the transactions were executed on a tax-deferred basis. Any taxes that remain payable on these transactions was offset through the application of unrecorded tax losses from prior years.

We ended 2015 with an investment portfolio, including holding company cash, of \$29 [ph] billion compared to \$26.2 billion at the end of 2014. The majority of the increase related to the consolidation of the portfolio investments of Brit and Fairfax India, partially offset by net unrealized depreciation of bonds and common stocks and the unfavorable impact of foreign currency translation.

Our debt-to-total capital ratio decreased to 21.8% at the end of 2015 from 24.6% at the end of 2014, primarily due to the increase in our total capital outpacing the increase in our total debt. The increase in total debt reflected the consolidation of the indebtedness of Brit, Cara and National Collateral Management, which was acquired by Fairfax India, and that was partially offset by the repayment of \$125 million of OdysseyRe senior notes in the second quarter and the repayment of \$82 million of Fairfax senior notes in the fourth quarter.

And now I'll pass it back over to you, Prem.

V. Prem Watsa

Founder, Chairman and Chief Executive Officer

Thank you, Dave. Now we're very happy to answer your questions. [Operator Instructions] So Jim, we're ready for the questions.

Question and Answer

Operator

[Operator Instructions] And now our first question comes from Junior Raj [ph] , an individual investor.

Unknown Shareholder

So I have a couple of quick questions. So one of the questions is your hedges that you've put on deflation itself, how do you see that playing out before 2022? And my other question would be, how do you see the BlackBerry investment working out in the future?

V. Prem Watsa

Founder, Chairman and Chief Executive Officer

Yes. So on the deflation swaps, deflation contracts that we put in, they've -- as I've said, it's almost 7 years yet to go. What we're trying to do is protect our company from worst case events, and deflation is a very difficult environment to make a return in. You're seeing interest rates in Japan, 10-year rates are negative. German rates are below -- 10-year German rates are below 0.3%, like below 0.3%, like 30 basis points for 10 years. So in that environment, it's very difficult to make a return, and we're trying to -- and there's all sorts of unintended consequences. And so we are protecting our company from that. And as far as BlackBerry, I've said for some time that we continue to be optimistic that John Chen, who's running the company, is going to do well over time.

Operator

And now our next question comes from Paul Holden from CIBC.

Paul David Holden

CIBC World Markets Inc., Research Division

So first question for you is in respect to the increase in interest and dividend income in 2015. So one of the comments from your press release is it was principally due to increased holdings of higher-yielding government bonds. So most insurance companies are kind of talking the opposite, that the average yield on their portfolios are going down. So just wondering where you're going within the sovereign credit spectrum to get a higher yield?

V. Prem Watsa

Founder, Chairman and Chief Executive Officer

Yes. So Paul, that's a very good question. First of all, we bought Brit, and Brit's got a \$4 billion investment portfolio that was added to our -- in the middle of -- somewhere in June, June 5, I think it was. So that's -- that whole portfolio has been added. One of the things we don't want to do in this environment is take credit risk. So when we acquired Brit, one of the first things we did was to eliminate credit risk and invest in government bonds, and in their case, U.S. government bonds in the main. But we do take duration risk. We buy long U.S. government bonds and so -- the increased size of the portfolio, plus the fact that we had U.S. treasuries, government bonds, would have increased our interest and dividend income.

Paul David Holden

CIBC World Markets Inc., Research Division

Got it. So you've gone a little bit further out on the yield curve.

V. Prem Watsa

Founder, Chairman and Chief Executive Officer

Yes.

Paul David Holden

CIBC World Markets Inc., Research Division

Yes, okay. Okay, that makes sense.

V. Prem Watsa

Founder, Chairman and Chief Executive Officer

We like that. I mean, just to give you a sense. Long government -- 3 or 4, 5 years ago, German bonds and U.S. government bonds were trading at the same rate, and many years before that, Japanese government bonds were also trading at the same rate. And they've all come down very significantly. The German bonds in the last 5 years have gone from maybe 3% or 4% to less than 1%. They're trading at 0.9%. These are for 30-year bonds. And U.S. government bonds have come down, but haven't come down as much. And in a deflationary environment, we expect them to come down also.

Paul David Holden

CIBC World Markets Inc., Research Division

Yes, yes. That's right. Canada, unfortunately, is getting a little bit closer to Europe as well. Anyways, next question, if I may. Just -- I have a question on ICICI Lombard. So the implied valuation you disclosed here is \$2.6 billion. The gross premiums written you disclose is \$1 billion for the year. So that implies a multiple of 2.6x of gross premiums written, not to say the best valuation metric but a valuation metric, and that's much higher than the 1.5x where Fairfax would be trading. So just wondering how you think about the valuation on that investment.

V. Prem Watsa

Founder, Chairman and Chief Executive Officer

Well, Paul, that's a very good question also. It wasn't cheap in terms of buying ICICI Lombard. It's the best company in India. We're very optimistic about the growth prospects of India. It's a company that -- it's the largest private company -- there's 4 government companies bigger, a little bigger -- but this is the largest private company. There's 350 branches represented all over the country. And India is very -- the penetration of insurance in India is very low, so the opportunity in ICICI Lombard is huge. So while -- if you compare our growth rates to ICICI Lombard, it began about 13 years ago with no premium, now in excess of USD 1 billion and it's just getting started. So we think there's -- the opportunity in terms of the future is why we agreed to pay a high price.

Operator

Our next question comes from Ron Bobman from Capital Returns.

Ronald David Bobman

Capital Returns Management, LLC

Congrats on the strong underwriting results. The Zenith numbers are impressive, and the Crum improvement is significant. I had a couple of inflation swap questions. My impression is that the inflation swaps are -- are sort of bespoke in nature, and so I'm wondering how you determine the market values at quarter end.

V. Prem Watsa

Founder, Chairman and Chief Executive Officer

Yes. So there's -- we have brokers, just like credit default swaps in the past, we have 2 brokers giving you a quote. And so very volatile, the quotes, but we get them, and we also have an internal model, which is very similar to the model that Wall Street uses in terms of modeling -- in terms of valuing these deflation swaps. So a combination of all of that, but we basically take outside quotes. David, that fair?

David J. Bonham

Chief Financial Officer and Vice President

That's absolutely correct, yes.

Ronald David Bobman

Capital Returns Management, LLC

And is it fair to say, generally, you've been satisfied with the quotes you've been receiving?

V. Prem Watsa

Founder, Chairman and Chief Executive Officer

Yes. It's really volatile. It's up and down, and we saw the same in credit default swaps. But I was looking back in our 2008 Annual Report, and you can see what I said there. But in 8 months, from June 2007 to February 2008, the valuation of our current deposit swaps went from \$200 million to \$2 billion. In 8 months, it went up 10x. And for 3 or 4 years prior to that, it did nothing. So these valuations, from what we see -- from where we sit, is -- it's in our books. We've taken a big hit in terms of our cost, and the next important number is when we sell it. And til that time, they're -- as you point out, valuations.

Ronald David Bobman

Capital Returns Management, LLC

My last question was you mentioned, Prem, in your prepared remarks, they've come to life in January '16. Could you give us some quantification of that?

V. Prem Watsa

Founder, Chairman and Chief Executive Officer

Well, a lot of the concerns that we've had for some time. And our experience over 40 years is you can never say when these concerns that we've had come to fruition, right? So for example, China. China, we've been worried about for many years, and their foreign exchange reserves have come down by \$1 whole billion -- \$1 trillion, as you know and that the foreign exchange market, the stock market, the bond market, the residential housing market, so all of those markets that they're trying to support. You've got Japan with negative interest rates, and the effect on banks is very significant. So bank stocks have dropped 30%-plus in Japan. But it's true also in Europe. So Deutsche Bank is making record lows, and it's due -- and it's also true in the United States. It's very difficult for banks to make money at very low interest rates. And so Japan is another problem that we're seeing. The United States had a -- the U.S., the fourth quarter that got reported in early 2016 was 0.7% annualized rate of expansion in the fourth quarter of 2015, a very low number, with all the QE1s, 2s and 3s and all of the other monetary expansion. And deflation, I just got the number for January. Deflation in the United States is 0%, it just came out today, like 0% deflation with all of the stimulus that we've had. The TIPS Spreads in the first 2 months, you know this is the spread between 10-year inflation bonds and 10-year treasuries, is now at about 1.25%, which is the lowest spread. And you have to go back to 2009, 2008 fourth quarter to see lower spread numbers, other than on the last week maybe they fluctuated a little bit. With that exception, you have to go way back. So -- and on top of that, you've got, as you know, record emerging market bonds that were issued in U.S. dollars. And you've got Venezuela, which has got more than \$185 billion, and most people are worried that they may not be able to pay. But these are owned in mutual fund structures in the United States. And if you have some defaults, that could cause significant problems because you've got record amounts, record amounts in emerging market debt in U.S. mutual funds. And then you know about what happened to the oil industry and the mining industry, and it's spreading into the utility industry. Dividends have been cut. So all of these things are taking place, and we worry that this isn't the -- cause of a deflationary environment. And it's coming to a head in the first few months in '16. It's already being reflected in the marketplace.

Ronald David Bobman

Capital Returns Management, LLC

But no number for the portfolios coming to life?

V. Prem Watsa

Founder, Chairman and Chief Executive Officer

No. We have longer-term rates, so we will look to 2016 reporting to you every quarter. We put it in the press release, so it's -- you don't have to take long to look and see what the values are. And so we'll update you every quarter.

Operator

Your next question comes from Jeff Fenwick from Cormark Securities.

Jeffrey Michael Fenwick

Cormark Securities Inc., Research Division

So Prem, I just wanted to follow up with that commentary of the slower outlook in the U.S. market. How should we be thinking about the U.S. P&C operations in that context? And then maybe we could go through a couple -- Zenith and Crum separately. I mean, Zenith certainly has had a very good cyclical upswing on improving employment in the U.S., but are we maybe entering a period of peak performance for Zenith, if that's the outlook from here? And how do you navigate that environment?

V. Prem Watsa

Founder, Chairman and Chief Executive Officer

So the U.S. property and casualty environment, as you know, is a soft environment. So our business, broadly speaking, is shrinking. Odyssey came down. We did not renew a major property account. The pricing wasn't right. So we're very focused on underwriting and our reserving, very important to keep the reserve being -- at a very good level. So that combination helps us navigate the soft market. But you're seeing some examples in the U.S. property, casualty industry where you've seen some pockets of under-reserving. You've had companies come and -- some big ones, some small ones, saying that they are under-reserved and they're taking reserve increases. Over time, that will have an impact. If -- there's been upsets for some time, there's been -- on the left-hand side of the balance sheet, there's been -- and many of our competitors have reached for yield and have taken credit risk to get more income, was one of the questions earlier. It's very difficult to get income. So they've gone up the credit risk curve. We think that's probably not an appropriate thing to do, and the spreads are very narrow. So the industry might turn some time, if some of the worries we have come to fruition. But day to day, we just try to focus on underwriting, and each of our companies are separately one. Our presidents are all very experienced. They know -- they're not worried about the top line. They're focused on the bottom line. And they think, over time, our results will continue to be excellent. Our underwriting -- since Andy took over in the last 4, 5 years, underwriting has really improved significantly, and it's disciplined, it's well-reserved and we feel very good about it.

Jeffrey Michael Fenwick

Cormark Securities Inc., Research Division

Okay. And I guess with that comment on reserve development, it's certainly been an important contributor for Fairfax over the last couple of years here. Can you give us the number, maybe in terms of points, on the combined ratio that would've been in Q4 for reserve development overall?

V. Prem Watsa

Founder, Chairman and Chief Executive Officer

Dave?

David J. Bonham

Chief Financial Officer and Vice President

Yes. Reserve development on a combined ratio point basis in the fourth quarter was 12.4%, fairly comparable to last year at 14.4%.

Jeffrey Michael Fenwick

Cormark Securities Inc., Research Division

And I would imagine that OdysseyRe had a fairly substantial number as well in the mix. Is that fair to say?

David J. Bonham

Chief Financial Officer and Vice President

Yes. OdysseyRe would have been relatively comparable to where it was last year at this time, too, in terms of reserve development, maybe a little higher, but comparable.

Operator

[Operator Instructions] And now the next question comes from Tom MacKinnon from BMO Capital.

Tom MacKinnon

BMO Capital Markets Equity Research

Just continuing on that discussion about fourth quarter. Dave, do you have what the fourth quarter cat losses were in terms of combined ratio points as well?

V. Prem Watsa

Founder, Chairman and Chief Executive Officer

Yes.

David J. Bonham

Chief Financial Officer and Vice President

Our fourth quarter cat losses were 1.3 combined ratio points, so about \$26 million.

Tom MacKinnon

BMO Capital Markets Equity Research

Okay. And then Prem, I noticed there were some realized bond losses in the quarter. Just wondering what they might be related to, if that's a sign of anything that we should be concerned about. Any color you can shed on that.

V. Prem Watsa

Founder, Chairman and Chief Executive Officer

No. They're just fluctuations. You know, Tom, that fluctuations in the -- in our bond portfolio -- if the interest rates went up a little, I don't know exactly what happened in the fourth quarter, but ...

Tom MacKinnon

BMO Capital Markets Equity Research

I'm talking the realized ones. You've realized some losses.

V. Prem Watsa

Founder, Chairman and Chief Executive Officer

In the fourth quarter, did you say?

Tom MacKinnon

BMO Capital Markets Equity Research

Yes.

David J. Bonham

Chief Financial Officer and Vice President

It was some of our Greek bonds that we sold in the fourth quarter.

V. Prem Watsa

Founder, Chairman and Chief Executive Officer

So we sold some Greek bonds in the fourth quarter.

David J. Bonham

Chief Financial Officer and Vice President

[indiscernible] basis had some realized losses.

Tom MacKinnon

BMO Capital Markets Equity Research

And what is the total holdings of your Greek bonds now then? And what were they at the third quarter? Just trying to get a feel for how much of the portfolio has been sold.

David J. Bonham

Chief Financial Officer and Vice President

I don't have the number off the top of my head, Tom, but it's not very much anymore in Greek bonds.

V. Prem Watsa

Founder, Chairman and Chief Executive Officer

We might have -- Tom, if memory serves me right, we have had something like \$150 million that we sold, and we might have \$150 million remaining approximately.

Operator

Our next question comes from Andrew Bell from BNN.

Andrew Bell

Prem, could I -- I hope you haven't dealt with this already. If your derivatives on CPI don't work out and if inflation comes back, seems unlikely right now, could you be on the hook for big losses? Is it a one-way bet here? Or could you actually lose money more than the \$600 million-odd that you put into these derivatives?

V. Prem Watsa

Founder, Chairman and Chief Executive Officer

No, Andrew. The way it works is we can only lose what we put into it. And in our statements at all, it's all mark-to-market. So I think at the end of December, it was \$270 million, something like that. So it's \$270 million. If inflation comes back -- these are about 7-year contracts. So if inflation continue -- comes back, as you say, and over the next 7 years, we could lose \$270 million. That's the limit. We can't lose anything more.

Andrew Bell

I'm sorry. Could I ask one last question? Just given some -- so these things last for another 6.6 years. So basically, does America and Europe have to be in deflation consistently for 6.6 years?

V. Prem Watsa

Founder, Chairman and Chief Executive Officer

Yes. It's an interesting instrument, and a good question, Andrew, but it's a cumulative inflation/deflation number that you have to look at over 6.6 years, 7 years on average. But the way it really works is it's also a marketable instrument, so there's a market in it. And of course, when there's no concern about deflation, then these contracts are selling at lower prices. And if there's fear of deflation or concerns about deflation, then these contracts can go up. That's what happens in these contracts, and so you don't really have to wait for 7 years before you realize on the contract.

Operator

Our next question comes from Sean Barry from RBC Dominion Securities.

Sean Barry

With respect to your concern about deflation, people like Dalio mentioned that another possible consequence might be currency wars, which we might sort of be in or beginning now. And of course, being such a global company now, we have a lot of foreign exchange. Do you people -- have you or your officers

sort of hedged that? Or how you -- or what are your concerns about that, if you have some? And then how do you protect the company going forward?

V. Prem Watsa

Founder, Chairman and Chief Executive Officer

That's a very good question, Sean. What we try to do, of course, is hedge our assets and liabilities. So if you've got assets in Canadian dollars, we've got -- our liabilities are in Canadian dollars, and so we hedge our Canadian dollar liability with Canadian dollar assets. We do that in the U.K., and we do that all over the place. What -- in Canada, we -- because we borrow in Canadian dollars, we can hedge a significant amount of our equity also at Fairfax. But in many countries, certainly smaller countries, the equity is exposed. So if we have 50 -- if you have \$200 million in -- I'm just using a number, in Singapore, for example, if you have close to \$400 million in Singapore, that equity in Singapore will not be hedged and so will our equity, our capital in all of the different countries, not be hedged. But in the big countries, we're all -- we're pretty well hedged.

Operator

Our next question comes from Mikel Abasolo from Solo Capital Management.

Mikel Abasolo

This has to do with your positions in Greece. Obviously, you're confident on the country coming back, given your last investment in Eurolife. But I was wondering if you could comment specifically on the investment that Fairfax reloaded on Eurobank. I believe that you bought shares in the placement at EUR 1 per share equivalent, and that has come down from -- quite a bit in the first few weeks of 2016. And if you can discuss that and what your stance is there, if you're considering increasing your stake in the bank, that would be of great help.

V. Prem Watsa

Founder, Chairman and Chief Executive Officer

Okay, Mikel, yes. So as far as Greece is concerned, we've said publicly that we think the present government recognizes that there's no alternative but to be in the euro and have demonstrated that by taking all the actions that the EU, the Troika has recommended. So they've -- so will be done something like 75% of all the recommendations, requirements for new money that the Troika has -- they put it in place. So we just think -- and they've done it quickly. And so we think the -- it's unlikely that they would leave the euro. That risk is very minimized. It's still there, but it's minimized. And we think -- Greece has come down 25% to 30% economically speaking. And when in -- housing, for example, in Greece is down something like 95%, 96%, so sales down 93%. So at the peak, if you had 100 houses being built, now you have 7 houses being built, right? So if 7 houses, you build 14 houses, that's a double, and you're still like 85% down. That's what happened in Ireland, and that's likely going to happen in Greece. So the -- when a country comes down so much, there's all these automatic stabilizers that come into play. And so we think the -- once a certain amount of political stability is maintained in Greece, that the economy will automatically come down, because it's gone down 25% to 30%. And as far as the Eurobank is concerned, it's -- the banking industry is consolidated from about 20 banks to 4. And with the recent financing, there's only 2 private banks, the first Eurobank and Alpha Bank. The other 2 have government money in it and certain restrictions that come with the government financing. Eurobank is really well run. We like the management team. We like their capital position. We think it's been -- it's recently been stress-tested, and so we think it's -- over time, we're long-term investors, we think Greece is going to do well and Eurobank is going to do well.

Operator

Our next question comes from Scott Heleniak from RBC Capital Markets.

Scott Gregory Heleniak

RBC Capital Markets, LLC, Research Division

I was just wondering if you could talk about the -- specifically, just the Eurolife transaction, if you could just walk through the opportunity you saw there on that particular deal. And then thoughts on -- along those lines, just the expansion that property -- brought you as far as on the life side and if that's something we should expect to see more of in the future versus P&C acquisitions.

V. Prem Watsa

Founder, Chairman and Chief Executive Officer

Yes. So just on the second part of your transaction, no, you're not going to see us expand in the life segment. It's just that this company has a very good management team. We like the management team. It's a separate unit. There's about 350 people, and they have a terrific track record. Half their earnings from property cash will be half their earnings from life, plain vanilla life; property combined ratios might be -- their property, casualty, P&C combined ratio might be below 70%. So they're excellent. Their reserving is very good. We happen to -- have come to know the management team for the last 3 or 4 years. And so -- and we are buying it, we think over time, at an attractive price, so basically, book value. And so all of those combinations suggested to us that this was an appropriate time to buy this company. And as I said, because of the management team, we think the prospects are excellent.

Operator

Our next question comes from Chris Lafayette from The Clark Estates.

Christopher Lafayette

I was wondering, in relation to the equity hedges, I assume that you would unwind them in certain scenarios. Can you talk a little bit about what metrics you look for in doing that? And are they macro-related or valuation-driven?

V. Prem Watsa

Founder, Chairman and Chief Executive Officer

Yes. So it's a combination. We bought these hedges to protect our company, right? So it's like the deflation swaps that we bought and Chris -- and the -- we're in a mark-to-market world. So if we wanted to expand our insurance business because prices are going up, but if the prices are going up in an environment where stock price are coming down, spreads are widening, well, our capital will be reduced significantly and so we may not be able to take advantage of the opportunity to increase our insurance business. So we protect our capital. In the 2008, 2009, the last time we did that, the markets came down about 50% and we took our hedges off. We just think we are facing -- in the insurance business, you think of it as a 1 in 50, 1 in 100-year storm, like not often, but you get these storms. You get an earthquake in California sometimes or you get a big windstorm in Florida. We've had many, and we have to protect ourselves from that. So it's a similar situation that we're looking at. We want to protect ourselves. And we think, right now, with the interest rates at 0 for some time and, in many cases, going negative and a ton of debt in the system, we think that the possibilities on the downside are significant. So we want to protect our company and we have no intention of taking those hedges off soon.

Operator

Our next question comes from Tom MacKinnon from BMO Capital.

Tom MacKinnon

BMO Capital Markets Equity Research

Just a follow-up question here, Prem. I think you've talked about a company target ROE, obviously, over the long run, of -- in the 15% range. If -- we've only hit it once in the last 7 years. In the last 7 years, it's averaged, as you know, probably closer to like a 5% or 6-ish range. So what would really be your -- what would you really need to do in order to move your ROE back up to that 15% target? Obviously, the underwriting results seem to be good. What would it take in order for you to, like over the long run, move towards that 15% target ROE?

V. Prem Watsa

Founder, Chairman and Chief Executive Officer

No. That's a good question, Tom. So our results over 30 years have been excellent because of 2 reasons. One is the focus on underwriting profitability. And in the last 5 years, our underwriting profitability has been the best it's ever been, if you look at 5-year periods. And last year, 2015 was the best in our history, as I mentioned to you. So the underwriting record is excellent, and it's sustainable in spite of -- we'll -- if there's a catastrophe someplace, somewhere, we'll get hit. I've mentioned that many times. But over time, I'm thinking long-term, our underwriting results are going to be excellent. We've got very good companies, very good presidents running it, all working with Andy Barnard. So that's doing well. In the last 5 years, investment results haven't been good. Our total returns have been in the 3% area, and over 30 years, our returns might have been 8.5% per year. So the 3% is by design, Tom, like we're worried. We want to survive. We don't want to be in a position where this company is going to be at risk of not surviving. So we'll take that poor result and not take a chance of not surviving. Let me give you a little example of that. In 2008, 2009, and I'm just using this because it's one that everyone knows, AIG had a 90-year track record of success; 90 years, and they built \$90 billion of capital over that 90 years, fantastic track record. One year, they disappeared and the U.S. government bailed them out to the tune of \$180 billion, something like that, and they survived. So we think of situations like that. In our company, we're not going to the Federal Reserve or the Bank of Canada or anyone else. So we're going to survive. We want to survive irrespective of what happens in the world. And so we'll take a lower return, and we have in the last 5 years, as you pointed out, and -- to make sure we survive. But the way we've structured our investment stock, like with these deflation swaps and our hedges and our 25% in our common shares, the way we've structured it -- and 2008, 2009 is a great example because in 2008, when most companies did not -- some didn't survive, most companies did very poorly, we did -- we had one of our better years. And then 2009, we had an outstanding year. Our book value in 2008, 2009 went up 61% cumulative. In '07, '08, '09, Tom, that's 2007, 2008, 2009, 3 years, our book value went up 146%, 146%. We think our investment portfolios are structured to provide that type of return if we get into problems. And we do not want to take a chance and try to meet quarterly or annual 15% hurdles and risk what we built over 30 years. So I'm giving you a sense for how we look at it. We, first, want to protect the downside, which we've done, we think. And then if things happen, we -- our company will do well. And so it's that combination. We've got 25% cash. No one's got cash. In 2008, 2009, the people who had cash took advantage of opportunity. Can I give you an example of that? You know about this. But at the fourth quarter 2008, fourth quarter 2008, the last quarter, there was \$4 billion approximately of Berkshire Hathaway guaranteed muni bonds that we bought and we still own, haven't sold a one of them, and we bought them in that last quarter at a 5.5% -- something like a 5.5% after tax yield, Berkshire Hathaway credit, more like 8% or 9% pretax yield. If you didn't, you can't buy 10 -- after that, you couldn't buy \$10 million worth of those bonds. You had to have the cash to take advantage of it, and we did. And so we've hedged our -- if we knew that the markets were going to go up, up and up and up, we should not have hedged and we'd have done extremely well. But as we keep saying to our shareholders, it's a 9-inning game. And you might be in the third or fourth or fifth innings, and it's not over yet. I've quoted in our Annual Report, wrong, wrong, wrong and then right, is better than the opposite.

Tom MacKinnon

BMO Capital Markets Equity Research

That's great, Prem. You mentioned -- you said you don't want to take a chance of not surviving. If -- as investors, what should we look at as being the key metric to follow in that case? Would that be just the holdco cash position? Is that the most important one for us to follow in terms of survivability chances, if you will?

V. Prem Watsa

Founder, Chairman and Chief Executive Officer

No, no. I think for us, Fairfax is an excellent position. No, no. I think we're in -- we're not making the returns. I was responding to your question on returns. But in terms of survivability, my suggestion to you is that very few companies would be as strong as ours. I mean, in some of the environments that we could be going into, Tom -- we came out of '08, '09 because the United States went all-in, took the interest rate down to 0% -- well, we're at 0% today. There's not a lot you can do in terms of debt because

they've already used a lot of their debt capacity. China went all-in maybe 2 or 3 times what the United States did. Well, China has less flexibility today. And interest rates are 0% all over the world. So if we go into a recession in the next year or 2, my suggestion is you're going to have all sorts of unintended consequences, and that's the worry we have, Tom. So our company is well structured for that. But if we muddle through like we have in the last few years, our returns are not going to be exceptional. They're going to be mediocre. We accept that with the idea that these are very difficult times and we have to be careful -- and I've said that to our shareholders, all of our shareholders at the telephone know that, especially our long-term shareholders, that we have to be very careful in this environment. Is there any more questions, Jim?

Operator

At this time, there are no further questions.

V. Prem Watsa

Founder, Chairman and Chief Executive Officer

Well, Jim, thank you very much. There are no more questions. Thank you all for joining on this call. We look forward to presenting to you again next quarter. Thank you, Jim.

Operator

You're welcome. That concludes today's conference. Thank you all for participating. You may now disconnect.

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