S&P Capital IQ

CONTENTS

Fairfax Financial Holdings Limited TSX:FFH

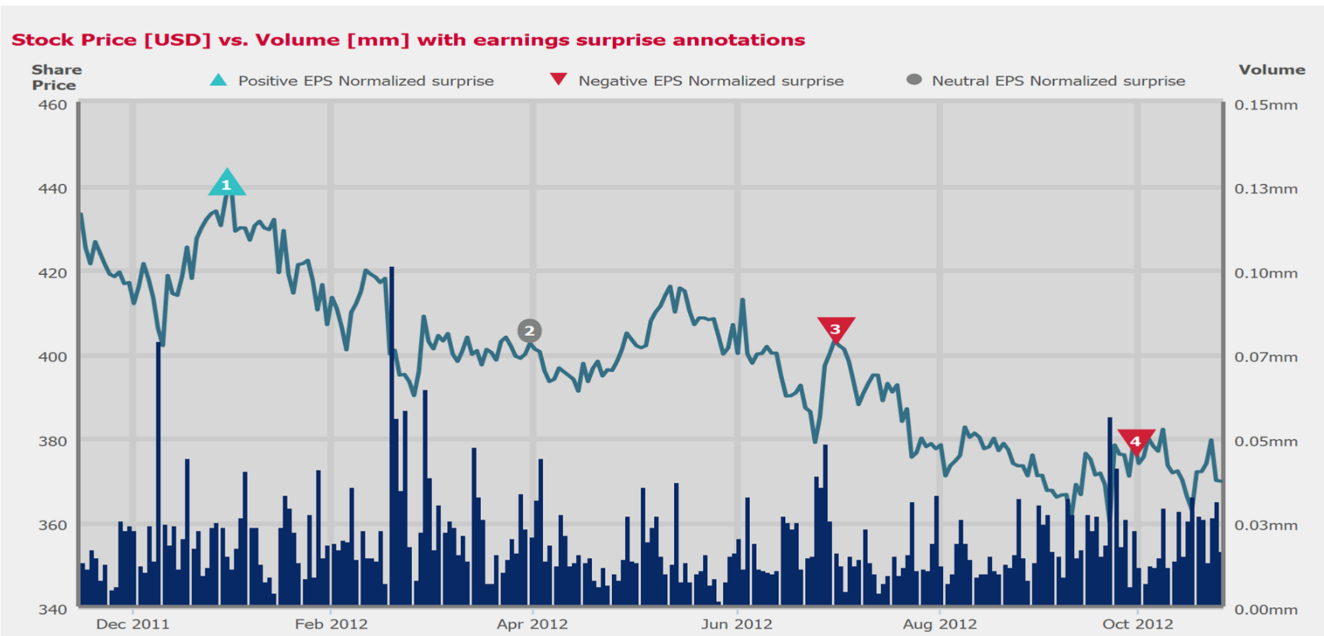
FY 2012 Earnings Call Transcripts

Friday, February 15, 2013 1:30 PM GMT

S&P Capital IQ Estimates

	-FQ4 2012-			-FQ1 2013-		
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	SURPRISE	CONSENSUS
EPS Normalized	4.73	18.90	▲299.58	1.12	▲73.24	8.94
Revenue (mm)	1640.35	1899.90	▲15.82	1888.70	▼(0.59 %)	7147.85

Currency: USD
Consensus as of Feb-15-2013 5:51 AM GMT



Call Participants

EXECUTIVES

David J. Bonham
Chief Financial Officer and Vice President

Paul C. Rivett
President

V. Prem Watsa
Founder, Chairman and Chief Executive Officer

ANALYSTS

Howard Flinker

Mark Alan Dwelle
RBC Capital Markets, LLC, Research Division

Paul David Holden
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Tim Piechowski
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Tom MacKinnon
BMO Capital Markets Equity Research

ATTENDEES

Unknown Attendee

Presentation

Operator

Good morning, and welcome to Fairfax' 2012 Year-End Results Conference Call. [Operator Instructions] 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 C. Rivett
President

Thank you, Catherine. Good morning, and welcome to our call to discuss Fairfax' 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.

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

V. Prem Watsa
Founder, Chairman and Chief Executive Officer

Thank you, Paul. Good morning, ladies and gentlemen. Welcome to Fairfax' 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 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, fourth worst year of catastrophe losses that we have experienced in our history. OdysseyRe, in spite of Hurricane Sandy, had outstanding result as its combined ratios 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, joint underwriting discipline with good reserves.

For you, our shareholders, the most important point to recognize is that in 2012, our Insurance and Reinsurance businesses continue to expand after being in a downturn for the 4 years prior to last year. In 2012, including the acquisitions we've made, net premiums written at Fairfax grew by 9.2%. Excluding acquisitions, which are First Mercury and PacificMas 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 losses 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 that there's 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 2 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 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 U.S. 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 of 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 runoff business of Brit Insurance Limited for $335.1 million, which was almost fully paid by the company's runoff 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 runoff subsidiary paid $200 million in full satisfaction of the 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 CAD 200 million of 5.84% notes due 2022, for net proceeds of approximately CAD 199 million. Early this year, on January 21, 2013, the company completed an additional CAD 250 million offering of its 5.84% notes due 2022, for net proceeds of CAD 258.1 million. These notes were priced 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?

David J. Bonham
Chief Financial Officer and Vice President

Thank you, Prem. First, I'll focus on Fairfax' 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 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 (sic) [$38.47] 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 that added 19 points to the combined ratio in that year.

In terms of reserves 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 benefit to 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 and 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. 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 a 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 to prior year's reserves, principally related to favorable emergence on prior year's catastrophe losses and casualty and property losses in the U.S. 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 U.S. 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; that compared to 107.9% in 2011. Excluding the reserve development we just mentioned, Crum & Forster's accident year combined ratio is 104.9% in the full year of 2012 compared to 104.2% in 2011.

Net premiums written by Crum & Forster in the full year of 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 Zenith's 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 priors year's reserves in 2012 compared to net adverse development to prior year's reserves, which added 6.8 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, those are 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 U.S. dollars. After adjusting for the transfer of the renewal rights to Northbridge's U.S. property book of business to an affiliate of OdysseyRe in May 2012 and adjusting for a nonrecurring 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 the 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 and underwriting profit of Fairfax Asia was 87% and $30 million, respectively -- or 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 development to prior year's reserves.

In runoff, Prem has highlighted many of the significant transactions that happened in runoff during the year. I'll round that out by saying that runoff 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 in dividend yield decreased to 1.63% for the year ended of 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 an improvement primarily due to increased shareholder's equity, that being the result of our 2012 net earnings, partially offset by common and preferred share dividends paid.

Then before I pass it back to Prem, I'd like to remind everyone that our Annual General Meeting will be held on Thursday, April the 11th, at 9:30 a.m. at Roy Thomson Hall. Details will be in the annual report on the last page, which will be published on March 8 in the evening.

So back to you, Prem.

V. Prem Watsa
Founder, Chairman and Chief Executive Officer
Thank you, Dave. And now, we are happy to answer your questions. [Operator Instructions] Okay, Catherine, we're ready for the questions.

Question and Answer

Operator

[Operator Instructions] And the first question is coming from Mr. Paul Holden, CIBC.

Paul David Holden
CIBC World Markets Inc., Research Division

Just want to ask 2 questions, if I may, and the first one is related to the trending cat losses. So historically, we've normally thought of cat losses as making up 4% to 5% of premiums earned, 5-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 differentials? Is pricing adequate now? I guess, my question is...

V. Prem Watsa
Founder, Chairman and Chief Executive Officer

Are you thinking in terms of our total return on capital, or investment returns, or what are you thinking about?

Paul David Holden
CIBC World Markets Inc., Research Division

I'm 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?

V. Prem Watsa
Founder, Chairman and Chief Executive Officer

Yes. So we look at that right now, and those percentages go up and down, as you know. But we think cat -- because of the recent catastrophes, so you've had the string of catastrophes in 2011 and you've 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. What that means is catastrophe pricing remains at very high levels, and we find that attractive. And subject to our limits, we are writing as much as we can 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 and not enough hurricanes, damage or earthquake damage that the pricing will be insufficient. But right now, it's attractive.

Paul David Holden
CIBC World Markets Inc., Research Division

Okay. And then second question's related to your equity hedges. And specifically, I want to hone in on sort of 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's a mismatch from an accounting basis because you don't mark-to-market those investments 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?

V. Prem Watsa
Founder, Chairman and Chief Executive Officer

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

Operator

Tom MacKinnon, BMO Capital.

Tom MacKinnon
BMO Capital Markets Equity Research

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 cat spaces. But the drag from being 31% invested in cash continues to kind of weigh on your operating results, if you will. What's it going to take for you -- or what sort of signals, or 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 be 31% invested in cash?

V. Prem Watsa
Founder, Chairman and Chief Executive Officer

That's a very good question, Tom. We've got about 30% cash, a significant amount of cash in the company. First of all, the -- 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? Well, 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 treasury are now comparable to what they were prior to 2008. And the economy, even last quarter, the United States was flat, or down 0.5%. So in spite of QE3, in spite of QE2, QE1, all of that massive stimulus, monitory 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, but we think what happened in the '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 a 100-year storm, so you have to be prepared for its after effects. We don't think it just lasted for 3 and 6 months, and so now we can go forward. And 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, in 2006. 2008, things turned the financial markets. Stock markets dropped, during that time, about 50%, and so we took our hedge off. And spreads widened significantly like really huge spreads. And Tom, the only people who could benefit from that were the people who had cash or government bonds. And so we are 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 3 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 they're many, so we are building cash. I did say, one last point, that in 2011 and 2012, we've realized, this is -- 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. And so we really think we're in a very good position, but always, with a long-term viewpoint, Tom.

Operator

From Mark Dwelle, RBC Capital Markets.

Mark Alan Dwelle
RBC Capital Markets, LLC, Research Division

A couple of questions, both related to the runoff 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 would be?

V. Prem Watsa
Founder, Chairman and Chief Executive Officer

Yes. So Eagle Star, Tom, was another deal that we did late in the year. So our annual report comes out, Tom, on March the 8th, and we'll give you a lot more details, not only, of course, on our runoff acquisitions, but also our views on the financial markets and that's sort of the opportunity to tell you a lot about some of these acquisitions. But runoff has done an outstanding job for us. Eagle Star's 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 runoff. They specialize in runoff, and so we just think that's a major advantage. There's very few companies that can do this, and there's maybe 2 or 3 companies that competes 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's 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?

David J. Bonham
Chief Financial Officer and Vice President

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

V. Prem Watsa
Founder, Chairman and Chief Executive Officer

Yes. And Mark, very similar to the businesses that we've done in the past. So we've got lots of experience, 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, and so our people would have a big advantage in knowing the details on these files.

Mark Alan Dwelle
RBC Capital Markets, LLC, Research Division

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

V. Prem Watsa
Founder, Chairman and Chief Executive Officer

Yes. Dave, you want to...

David J. Bonham
Chief Financial Officer and Vice President

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 runoff, and that will peter out over the next 9 months to 12 months and there shouldn't be any more premium coming in through there.

Mark Alan Dwelle
RBC Capital Markets, LLC, Research Division

So it should taper down from sort of $30 million -- $30 million was the earned in the fourth quarter. So it should taper down to -- from there to sort of nothing over the next 9 months, give or take?

V. Prem Watsa
Founder, Chairman and Chief Executive Officer

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 reserves and bring them back as we get more familiar with the reserving practices, the reserving claim funds, 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.

Mark Alan Dwelle
RBC Capital Markets, LLC, Research Division

That definitely brought a lot of assets to bear on the balance sheet and if you're successful investment in that should go a long way. So good luck with that one. Those are all my questions.

Operator

The next question is coming from Howard Flinker of Flinker & Company.

Howard Flinker

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

V. Prem Watsa
Founder, Chairman and Chief Executive Officer

Just a little louder, Howard.

Howard Flinker

Is there a difference between net premiums written in the income statements and in the -- there are short table, the runoff?

V. Prem Watsa
Founder, Chairman and Chief Executive Officer

Yes. Dave, can you...

David J. Bonham
Chief Financial Officer and Vice President

Yes. Can you just elaborate a bit more there, Howard?

Howard Flinker

Yes. In that table where you have divisional premiums written, using the fourth quarter, the premiums written totaled $1,399 million and in the income statement, the premiums were $1,598 million, talking net premiums.

V. Prem Watsa
Founder, Chairman and Chief Executive Officer

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

Howard Flinker

Fair enough. That's my question.

Operator

The next question is coming from Tim Piechowski, ACR.

Tim Piechowski
Alpine Investment Management, LLC

This is for [indiscernible] I guess, at this point the company has outstanding kind of CAD 2.6 billion worth of preferred and debentures. And I guess my question would be kind of, given that Northbridge's kind of continuing to increase premiums written, how much of that CAD 2.6 billion outstanding you guys think of as, I guess, a hedge for Northbridge and other Canadian operations versus kind of a short position due to the Canadian dollar or results [ph] economies generally?

V. Prem Watsa
Founder, Chairman and Chief Executive Officer

No, 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, the capital -- Dave, what's Northbridge's capital?

David J. Bonham
Chief Financial Officer and Vice President

Say about $1.3 billion.

V. Prem Watsa
Founder, Chairman and Chief Executive Officer

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

David J. Bonham
Chief Financial Officer and Vice President

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.

Operator

The next question is coming from Shehzad Okkai [ph], a private investor.

Unknown Attendee

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, I guess, unseen levels, 70% or 80% above historic averages. We're still at a very high Shiller P/E ratio when you look at over -- when you look at earnings over the last 10 years. And as you mentioned earlier, lows in corporate bond yields, particularly junk yields, so margin of safety seems to be very low, but as a 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, very large U.S. deficits. So are we in a position where this could -- where the situation could really persist for a long time going forward?

V. Prem Watsa
Founder, Chairman and Chief Executive Officer

Shehzad [ph], 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, Shehzad [ph], in the March 8th 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 free -- nice free discussion. But really, when this will change, Shehzad [ph], really no one knows. Our view is that we have to be very strong financially. 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, very, conscious of the downside. And while, at the same time, looking for opportunity, and we've -- and we are finding quite of bit and we're realizing quite a bit of gains as I have mentioned to you. So it's a fine balance and we watch that very carefully every day.

Operator

We have no further questions at this time.

V. Prem Watsa
Founder, Chairman and Chief Executive Officer

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 in our Annual Meeting on April the 11th. Thank you.

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