Fairfax Financial

Hiding in Plain Sight

A collection of posts from an investor on the
'Corner of Berkshire & Fairfax' investing forum.

Updated April 8, 2024

With thanks to current and past investors who post(ed)
on the Corner of Berkshire & Fairfax investing forum.
The wisdom provided over the years has been life-changing
for me and my family. A special shout-out to Sanjeev Parsad,
who founded the forum 20 years ago and still manages it today.

Thank you.

Viking
(Lars Nordal)

Table of Contents

Introduction

What follows is a collection of more than 80 posts, most of which were written over the past twelve months. Many of the individual posts read like an essay – a short article on a particular subject. The 'subject' is a little followed, misunderstood, scrappy insurance company called Fairfax Financial.

My intent in publishing this document is to inform and entertain. **This is NOT intended to be financial advice** (more on this topic later). It is impossible to know everything about a subject. At times, this makes it necessary for the author to try and 'fill in the blanks.' Therefore, when telling this story, the use of some creative license is necessary.

My Fairfax Journey

I have followed Fairfax for about 20 years, buying my first shares in 2003. I am not a buy and hold investor. I buy when the shares are cheap, and concentrate when the shares get 'crazy' cheap. And I lighten up when the shares go higher and become more fully valued. I did this first with Fairfax in 2003 and again in 2006-09. And now for a third time from late 2020-present. I was largely out of the stock from 2010-2018, because I did not like what Fairfax was doing with their investments.

I was able to semi-retire (quit my day job!) at the age of 40, largely due to the gains over the years from my different investments in Fairfax. Over the years, I have invested in numerous other stocks and have done reasonably well with them. But my outperformance has been mostly driven by Fairfax (owning a concentrated position in Apple from 2013-15 also helped). As a result, Fairfax has a special place in my heart and this likely affects my views on the company.

I own Fairfax shares (April 8, 2024). As I stated above, I am normally not a buy and hold investor. So, as you read this document, I may have already sold some or all of my shares in the company.

Why post so much on one company?

One word: concentration. The outperformance of many successful investors is often driven by a couple of concentrated bets (to learn more, research investor Stanley Druckenmiller). But concentration only works if you have a very good understanding of the company and its situation. And you are right. For this to happen you have to put in the work. There are no short cuts - hence why concentration is a terrible strategy for most investors. What is contained in this document is some of the work that I have put in over the past 36 months to try and better understand Fairfax.

Corner of Berkshire and Fairfax: https://thecobf.com

I have had lots of help along the way. I have been a member of the investing forum Corner of Berkshire and Fairfax since 2003 - this is where I got the idea to invest in Fairfax in the first place. The investing forum has been an invaluable resource to communicate and debate ideas - think/write/discuss - often in real time as events happen. I have been able to tap into the collective wisdom of its extensive membership - learning more about Fairfax and investing in general. It has been a life changing experience for me and my family.

So, a big "thank you" to the investor community at the Corner of Berkshire and Fairfax for all their help over the years. A shout-out to @glider3834 (Tarn Crowe) and @nwoodman, both of whom are blood-hounds with finding and posting links to interesting and useful information on Fairfax and its many subs. Much of the collective wisdom of this group has found its way into this document.

Why was this document created?

I like to write long-form posts. I also post quite frequently. Given how much digital ink I had spilt writing about Fairfax, I decided I needed to keep track of my posts more carefully. About 18 months ago, I started keeping them in a Word document. The posts kept coming and soon I had more than 100 pages of material, which became more than a little unruly. I decided to organize everything into several broad topics, which became chapters. Then I decided it would be useful to edit the entire document to make it more readable. What emerged is what you are reading here.

Warning: it is a bit of a Frankenstein document.

I did not write individual posts with the idea of folding everything into one document. The topics of the posts varied greatly. Sometimes I wanted to learn about a specific part of the company so I would do a deep dive. Other times, I would step back and look at Fairfax from a distance. Lots of posts were inspired by current events. I am also a bit of a history buff so a large number of posts dig into Fairfax's past. I have also included numerous source material (quotes and links) so readers can make up their own minds – they do not need to rely on my interpretation of events.

How is the material organized?

The material has been organized into sixteen chapters. Each individual post is listed in the Table of Contents which makes it easier for the reader to identify topics of that might be of interest. And for ease of readership, with a simple click or tap, the individual posts can be accessed directly from the Table of Contents via a hyperlink.

The posts sometimes contain material that crosses over to other Chapters so the organization is loose at best. The posts can also be a little repetitive. To help make the document more readable, some of the posts have been edited or updated. Bottom line, as editor, I have done as I saw fit.

The fundamental flaw of compiling a collection of old posts

Despite some editing, most posts have been copied largely as they were originally written. I have included the date they were posted to provide the reader with much needed context. This is very important because, to state the obvious, things are constantly changing at Fairfax, in the P/C insurance industry, the economy, with the weather (think hurricanes) etc. And every 90 days we get a new earnings release from the company.

As a result, the underlying fundamentals at Fairfax are constantly changing. I usually update my models every couple of weeks - and incorporate new information. However, these important changes do not make their way into old posts – only new posts. **What the reader is getting with**

each post is a glimpse into what I was thinking about Fairfax and the topic being written on that date – not what I think about Fairfax and the topic today.

There are other important shortcomings with this document that the reader should be aware of.

<u>1.) I like to forecast (that is another word for guess).</u>

But my crystal ball is no clearer than that of the average person. **All of my forecasts in older posts are already wrong. And my forecasts in newer posts will be wrong soon.** That is the nature of forecasts – they are simply a best guess at a point in time. As time moves forward and new information becomes available then old forecasts become obsolete. (Before you decide to stop reading this document - most of my forecasts on Fairfax over the past two years have been wrong - because they have been too conservative.)

<u>2.) I have opinions on lots of things.</u>

And I am sometimes wrong. But I do not know where I am wrong (or I would change it). The reader needs to examine this document with a high degree of skepticism. As well, my opinions on many topics are constantly evolving. The reader needs to keep this in mind.

<u>3.) Most importantly, I know my understanding of Fairfax is flawed</u>

To state the obvious, the management team at Fairfax was not involved in any of this document. I have contacted the company directly only one time ever (to ask a very inane question about Sanmar – a company in Fairfax India's portfolio). I did attend the AGM in April of 2023 - where I asked one question. **As a result, I have an outsider's perspective and this means my 'interpretation' of historical events and analysis of the company is going to contain errors.**

<u>4.) A message from the legal department</u>:

This document contains lots of errors. It is also full of opinions that may or may not be accurate. I do not have an insurance background. Or an accounting background. I have never worked in the investment or banking industries. And I am not a writer. **Most importantly, this document is NOT intended to be investment advice**. **Consult a professional investment adviser before making any investment decisions.** To state the obvious, making investment decisions based on the ramblings of some person who posts anonymously on an investing forum could be disastrous.

<u>Conclusion</u>

My goal with this document is to provide a broad collection of writings on Fairfax that weave a story of the company – its past, present and future. Hopefully it also educates and entertains along the way and motivates you to want to learn more.

Viking (Lars Nordal)
April 8, 2024

<u>Note</u>: Unless otherwise noted, all numbers in this document are in US$

Chapter 1: An Overview of Fairfax

This document is NOT your best source of information on Fairfax. The best source of information on Fairfax is, of course, the company's web site: https://www.fairfax.ca

I have put many of what I consider to be the best posts in Chapter 1. Each covers a different part of the company. Together, they begin to tell the story of what I like to call the 'new Fairfax.'

If you are time constrained, start with the posts in this chapter.

An Introduction to Fairfax

Below are some links from the company's web site to get you started.

Overview of the Company: PowerPoint Presentation from the Fairfax AGM – April 2023

https://www.fairfax.ca/wp-content/uploads/Fairfax-AGM-2023.pdf

The Year in Review: Prem's Letter from the 2023 Annual Report

https://www.fairfax.ca/wp-content/uploads/FFH_Fairfax-Financial-Shareholders-Letter-2023.pdf

Recent Earning Report: News release for Financial Results for Year-End 2023:

https://www.fairfax.ca/press-releases/financial-results-for-the-third-quarter-2024-02-15/

2023 Annual Report

https://www.fairfax.ca/wp-content/uploads/FFH_Fairfax-Financial-2023-Annual-Report.pdf

Fairfax Financial and Margin of Safety

Updated April 3, 2024

"The three most important words in investing are margin of safety." *Warren Buffett*

Ben Graham introduced 'margin of safety' as the central concept of investing in Chapter 20 of his book, The Intelligent Investor. The idea is to only purchase stocks when they are trading at significantly less than their intrinsic value (buy something for $0.50 that is worth $1.00). This approach limits your downside if you are wrong and it provides significant upside if you are right.

A lot has happened at Fairfax over the past 3 years. Let's do a top-line review and see what we can learn about the company's current stock valuation.

First, let's get some context.

<u>How has Fairfax's stock performed over the past 3.25 years?</u>

Fairfax has been one of the best performing stocks over the past 3.25 years both in absolute and relative terms. From Dec 31, 2020 to Mar 31, 2024, Fairfax's stock is up a total of 216% while the S&P500 is up 40, which has resulted in outperformance of 176%. That record of outperformance makes Fairfax one of the best performing large-cap stocks in Canada over this time frame.

Fairfax (US$)	Share Price	YOY change			S&P500	YOY change	
Dec 31, 2020	$341		increase		3,756		increase
Dec 31, 2021	$492	44%	over		4,766	27%	over
Dec 31, 2022	$594	21%	past 39		3,840	-19%	past 39
Dec 31, 2023	$921	55%	months		4,770	24%	months
Mar 31, 2024	$1,079	17%	216%		5,254	10%	40%

For context, Fairfax is the 31st largest Canadian company based on market cap (at Mar 31, 2024).
https://companiesmarketcap.com/canada/largest-companies-in-canada-by-market-cap/

After such a big increase over the past three years, does this mean Fairfax's stock is now expensive? The proverbial 'big fish that got away' from investors? Maybe. But before we jump to any conclusions, what do the traditional valuation measures tell us?

<u>Price-to-earnings ratio (PE)</u>

Fairfax's trailing PE multiple is 6.2x, which is very low.

Fairfax	
Share Price - March 31, 2024	$1,079
2023 Reported Diluted EPS	$173
PE Ratio	6.2

Compared to peers, Fairfax's PE multiple is at a significant discount. Fairfax's PE multiple is at a 40% discount to Markel (low) and at an 80% discount to Intact Financial (high).

P/C Peer Comparison PE Multiple	PE	Fairfax Discount To Peers	Share Price March 31 2024	2023 Reported Earnings
Fairfax	6.2		$1,079.04	$173.24
Markel	10.4	40%	$1,521.48	$146.98
Chubb	11.9	48%	$259.13	$21.80
WR Berkley	17.5	64%	$88.17	$5.05
Intact (C$)	31.5	80%	$220.04	$6.99

What is the PE multiple of the overall market? The PE multiple of the S&P500 is over 20. Fairfax's PE multiple is less than 1/3rd the multiple of the S&P500.

Looking at PE multiple, Fairfax's stock looks like it is trading at a severe discount compared to both P/C insurance peers and the S&P500.

Return on equity and price-to-book value

Return-on-equity (ROE) and price-to-book value (P/BV) are the preferred metrics to use to value P/C insurance companies. Let's start with ROE.

What did Fairfax deliver in 2023? How does it compare to peers?

Fairfax delivered an ROE of 21.7% in 2023, which is outstanding. This performance is better than the peer companies listed below. (Yes, my calculation method is crude. At this stage of our analysis, we simply want to get a quick/rough snapshot of key metrics.)

P/C Peer Comparison Return on Equity	ROE (1)	2023 Reported Earnings	Book Value December 31 2023	Book Value December 31 2022
Fairfax	21.7%	$173.24	$939.95	$657.68
WR Berkley	18.5%	$5.05	$29.06	$25.52
Chubb	16.2%	$21.80	$146.83	$121.90
Markel	14.5%	$146.98	$1,095.95	$929.27
Intact (C$)	8.6%	$6.99	$81.72	$80.33

(1) ROE is calculated using average BV.

How about P/BV?

Fairfax's P/BV is 1.15. This is a low multiple and usually applied to P/C insurers that are generally considered to be lower quality / poor investments.

Fairfax's P/BV multiple is at a significant discount compared to peers. Fairfax's P/BV multiple is at a 17% discount to Markel (low) and at a 62% discount to WR Berkley (high).

P/C Peer Comparison P/BV Multiple	P/BV	Fairfax Discount To Peers	Share Price March 31 2024	BV 2023YE
Fairfax	1.15		$1,079.04	$939.95
Markel	1.4	17%	$1,521.48	$1,095.95
Chubb	1.8	35%	$259.13	$146.83
Intact (C$)	2.7	57%	$220.04	$81.72
WR Berkley	3.0	62%	$88.17	$29.06

Given Fairfax delivered a 21.7% ROE, the fact the stock is trading at a P/BV of 1.15 makes no sense.

Is poor past performance the issue?

<u>Book value per share (BVPS)</u>

Let's look at the change in BVPS for the past 5 years - from December 31, 2018 to December 31, 2023. How much has BVPS increased at Fairfax? How does Fairfax's performance compare to other P/C insurance peers?

Over the past 5 years, BVPS has increased at Fairfax by 117%, which is a CAGR of 16.8%. Fairfax has also paid a dividend each year. That is very good performance. And it is significantly better than the peer companies listed below.

P/C Peer Comparison	Dec 31 2023	Dec 31 2018	Book Value Per Share		
	BV per Share		5 Year Change		Approx
			$	%	CAGR
Fairfax	$939.95	$432.46	$507.49	117%	16.8%
Markel	$1,095.95	$653.85	$442.10	68%	10.9%
Intact Financial (C$)	$81.72	$48.73	$32.99	68%	10.9%
WR Berkley	$29.06	$19.81	$9.25	47%	8.0%
Chubb	$146.83	$109.56	$37.27	34%	6.0%

Note: All companies pay a dividend except Markel.

What can we conclude after taking a quick look at some basic valuation metrics?

Fairfax has delivered:

- Top-tier ROE of 21.7% in 2023.
- Top-tier CAGR in BVPS of 16.8% over the past 5 years.

And yet, Fairfax's stock trades at very low valuation multiples:

- PE = 6.2
- P/BV = 1.15

What is the problem? Is there an issue with earnings quality or the future prospects of the company?

Let's keep digging.

What about quality of Fairfax's earnings?

The quality of the earnings being delivered by Fairfax in 2023 are the highest in the company's history - it is primarily being delivered by record operating earnings: underwriting profit + interest and dividend income + share of profit of associates. All three - on their own - are at/near record levels. So earnings quality is high.

What about the future prospects for Fairfax?

Fairfax has three economic engines driving its business:

- Insurance: Over the past 9 years, Fairfax has grown net premiums written by 274%. This has been driven by acquisitions and, in recent years, the hard market in insurance. In 2023, Fairfax delivered net premiums written of $22.9 billion and an underwriting profit of $1.5. Bottom line, Fairfax's insurance businesses have never been positioned better.
- Investments - fixed income: Over the past 3 years, the fixed income team at Fairfax has superbly navigated Fairfax through the greatest bond bubble/bear market in history. In 2023 they extended the average duration of the fixed income portfolio to more than three years. Fairfax is poised to earn +$2 billion in interest income in each of the next three years.
- Investments - equities: Over the past 5 years, Fairfax's $19 billion equity portfolio has been slowly increasing in overall quality - new purchases have been very good and old problems have largely been fixed. The portfolio of holdings is performing well, led by Eurobank and the FFH-total return swaps (giving them exposure to 1.96 million Fairfax shares). The higher quality of the total portfolio should result in higher future returns.

Most importantly, all three of Fairfax's economic engines are performing very well at the same time. Significant asset sales over the past 18 months have been icing on the cake: pet insurance (for $1.4 billion), Resolute Forest Products (for $626 million + $183 million CVR) and Ambridge Partners (for $379 million).

In short, Fairfax's prospects have rarely looked better. As a result, record operating earnings (and earnings overall) are expected to continue in the coming years.

What about management?

I wrote a long-form post that reviewed capital allocation at Fairfax over the past five years. (See the next post in this chapter.) Bottom line, it can be convincingly argued that Fairfax has a best-in-class management team compared to P/C insurance peers.

What are external groups saying?

AM Best, the credit ratings agency who specializes in insurance companies, upgraded Fairfax's ratings (including those of its two largest subs - Odyssey and Allied) in 2023, because of its improved financial profile.

Most sell-side analysts have been warming to Fairfax over the past year, repeatedly increasing their estimates and target prices. Most have Fairfax rated as 'outperform.'

Conclusion

What did we learn about Fairfax?

Fairfax is a well-managed high-quality company with solid prospects that appears to be trading at a large discount to P/C insurance peers and the overall market.

Despite the big move the past 3.25 years, in Ben Graham's parlance, Fairfax's shares appear to be trading today with a large margin of safety.

Capital Allocation - Is the Management Team at Fairfax Best-In-Class?

Updated April 3, 2024

Capital allocation is the most important responsibility of a management team. Why? Capital allocation decisions are what drive the long-term performance of a company and important metrics like reported earnings, growth in book value and return on equity. In turn, these metrics drive the multiple given to the stock by Mr. Market - and finally the share price and investment returns for shareholders.

Capital allocation is especially important for P/C insurance companies. And that is because of something called float – which provides low cost (sometimes free) leverage (see Chapter 4).

When done well, capital allocation does two important things:

1. Delivers a solid return.
2. Improves the quality of the company.

Therefore, the fundamental task of an investor is to determine if management, over time, is making intelligent decisions regarding capital allocation.

<u>What is capital allocation?</u>

Capital allocation is the process of determining how capital is raised, managed and disbursed by a company. Capital allocation decisions often play out with a lag, sometimes years in length. Recognizing this, an investor needs to take a multi-year approach with their analysis.

<u>What are the sources of capital for Fairfax?</u>

Fairfax has three sources of capital: equity (common shareholder's + preferred stock), debt (holding company) and float. The largest bucket is the $35.1 billion in float which has a cost of less than zero - because they earn an underwriting profit (over the past 10 years Fairfax has averaged a CR of 95.5%). Fairfax also utilizes some debt, which has an average cost of about 5%.

All together Fairfax has total capital of about $65 billion working for shareholders, or about $2,825/share. This capital has been obtained at a very low average cost.

Fairfax: Sources of Capital (very rough calculation)		
	$bn	
Sharholders Equity	$23.0	Dec 31, 2023
Hold Co Debt (liability)	$6.9	Dec 31, 2023
Float (liability)	$35.1	Dec 31, 2023
Total Capital	**$65.0**	
Shares Outstanding (mn)	23.0	Dec 31, 2023
Capital per Fairfax Share	$2,825	

How does Fairfax do capital allocation?

Internal capabilities: Capital allocation at Fairfax is managed by the senior leadership team, led by CEO Prem Watsa.

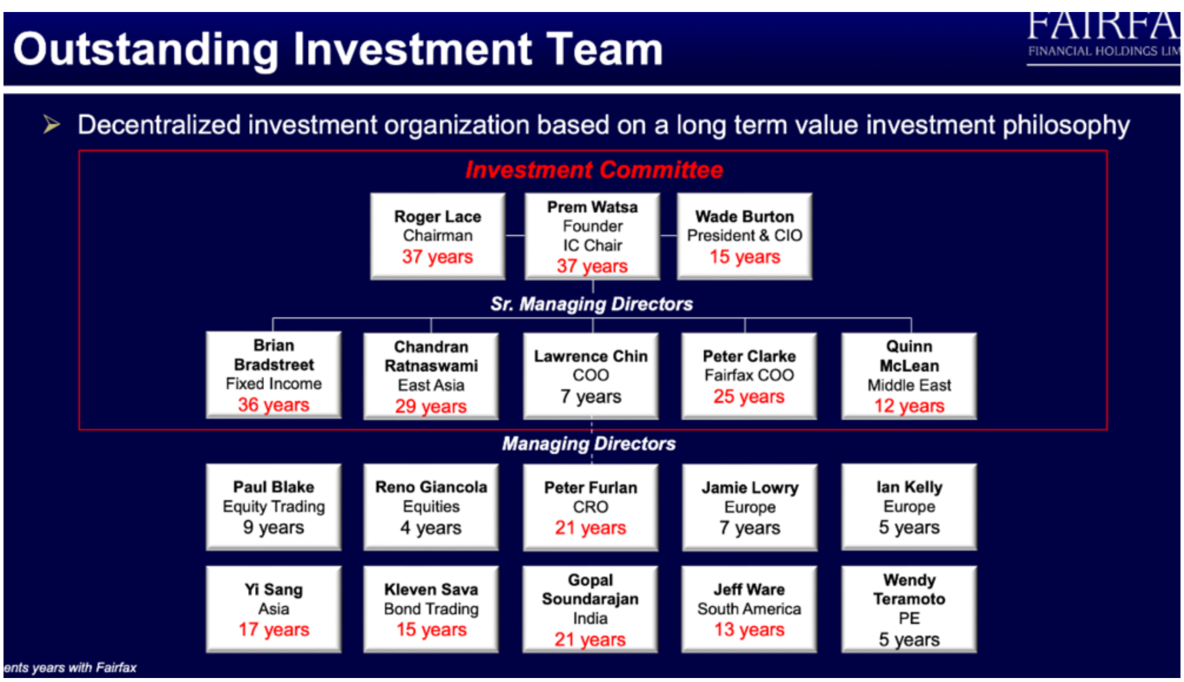
- Insurance: Since 2011, the insurance business has been led by Andy Barnard. In early 2023, Brian Young was promoted and now shares oversight responsibilities with Andy Barnard over all of Fairfax's insurance and reinsurance operations. Brian is also still CEO of Odyssey.
- Investments: The investment business is managed by the team at Hamblin Watsa.
    - The fixed income team is led by Brian Bradstreet, who has been with Fairfax from the beginning.
    - The equities team is led by Wade Burton, who joined Fairfax in 2009 from fund manager Cundill Investments, and Lawrence Chin, who joined from Cundill in 2016.
    - In India, Fairfax has Fairbridge, a boots-on-the-ground investment team.

Fairfax also leverages the knowledge of the many CEO's who manage their vast collection of equity holdings across the globe.

"Since 1985, investments have been centrally managed for all of the Fairfax group companies by Hamblin Watsa Investment Counsel Ltd. (www.hwic.ca), a wholly-owned subsidiary of Fairfax. Hamblin Watsa emphasizes a conservative value investment philosophy, seeking to invest assets on a total return basis, which includes realized and unrealized gains over the long-term." *Fairfax web site*

Fairfax has a large internal team with expertise across many different asset classes and geographies. They are a long-tenured group with experience managing through many different market cycles. They are also a battle tested team. They have established a strong long-term track record of success.

Below is a slide from the AGM (April 2023) that summarizes Fairfax's internal investment team.



This document is not intended to be financial advice. Its purpose is to educate and entertain. Amounts are in US$.

External capabilities: Fairfax has been actively cultivating relationships with a large network of individuals/companies in the investment world for decades. The company has established partnerships and expertise across many different asset classes (real estate, private equity, commodities) and geographies (India, Greece, Africa, the Middle East). These external partnerships have been an important source of ideas and diversification while also delivering solid returns to Fairfax over the years. This important external capability allows Fairfax to leverage the knowledge and skills of a much larger group of people and organizations.

Summary: Over decades, Fairfax has built out a large team and network of highly skilled internal and external capital allocators. **In a world where active management is back, this has become a significant competitive advantage. Fairfax is well positioned at exactly the right time.**

In general, what are the basic capital allocation options available to management?

- Reinvest in the business - grow organically: support the slow and steady growth of existing operations.
- Acquisitions/mergers - higher risk, but can be transformative.
- Asset sales - lower risk, opportunity to take advantage of Mr. Market (sell high).
- Pay down debt: the most predictable option, as the cost of repaid debt is known.
- Pay dividends: although tax-inefficient, usually indicates a financially healthy, shareholder-friendly company.
- Share buybacks: impactful, if purchased below intrinsic value, by improving per-share financial metrics like earnings per share and book value per share.

What has Fairfax done?

The management team at Fairfax has been extremely active on the capital allocation front. Every year they typically make from five to ten meaningful decisions. So much has been happening on the capital allocation front in recent years it is hard for shareholders to keep up - especially understanding the impact on future business results. Below we are going to take a quick look at 16 of Fairfax's bigger decisions made in recent years to see what we can learn.

Reinvest in the business:

1.) 2019-2023, hard market in insurance. Net premiums written have increased a total of 73% over the past four years from $13.3 billion in 2019 to $22.9 billion in 2023, a CAGR of 14.6% per year. In 2023 Fairfax delivered a record underwriting profit of $1.5 billion (the CR was 93.2%).

2.) In 2017, seeded start-up Go Digit in India at a cost of $154 million. Fair value at December 31, 2023 was $2.265 billion. This investment has turned into a home run, with a possible IPO coming in 2024 (bringing more potential gains).

Acquisitions/sales: insurance:

3.) In 2017, purchased Allied World, with the help of minority partners, for $4.9 billion (at 1.3 x book value). The price paid was not an overpay. Net written premiums have increased from $2.37 billion in 2018 to $4.84 billion in 2023, an increase of 104% in 5 years. With the onset of hard market in 2019, the timing of this purchase was perfect.

4.) <u>In 2017/2019, sold ICICI Lombard for $1.7 billion</u>: realized a $1 billion pre-tax investment gain. Due to regulations in India, Fairfax had to sell down its position in ICICI Lombard to be able to invest in Digit. This action was a brilliant strategic shift of Fairfax's insurance business in India.

5.) <u>In 2020/2021, sold Riverstone UK (runoff) for $1.3 billion</u> (plus $236 million CVI). At a time when they needed the cash, Fairfax sold their UK run-off business at a much higher price than expected at the time. By shrinking the size of the runoff group, this sale also improved the overall quality of the remaining P/C insurance businesses.

6.) <u>In 2022, sold the pet insurance business to JAB Holding Co. for $1.4 billion</u>. This action resulted in a $1 billion after-tax gain. This sale was a home run for Fairfax as the business was sold for a much higher price than anyone thought possible (most people didn't even know Fairfax owned this business).

7.) <u>In 2023, purchased KIPCO's 46% stake in Gulf Insurance Group for $740 million</u> fair value consideration, as it is payable over 4 years. Fairfax paid a premium to get a control position in a quality business. This is a great strategic purchase that will solidify Fairfax's presence in MENA region for insurance. This deal closed in late December 2023.

<u>Acquisitions/sales: investments</u>:

8.) <u>In 2018, made initial investment in Poseidon/Atlas/Seaspan</u>. Fairfax partnered with David Sokol (formerly Buffett's heir apparent at Berkshire). Today Fairfax owns a 43% stake in this company with a market value of $2.046 billion at December 31, 2023. Poseidon will see significant growth in 2024 as it takes delivery of a large number of container ships and completes the final leg of its multi-year new-build strategy.

9.) <u>In late 2018, purchased 13.7% of Stelco for $193 million</u>. Fairfax partnered with Alan Kestenbaum. Since 2018, Stelco has paid Fairfax $106 million in dividends. Over the past 3 years, Stelco has repurchased 38% of total shares outstanding. Today, Fairfax now owns 23.6% of Stelco (having invested no new money). Fairfax is exceptionally well positioned for when the next bull market in steel happens.

10.) <u>In 2020/21, initiated a total return swap position giving them exposure to 1.96 million FFH shares</u> at an average cost of $373/share. With Fairfax's stock closing at $1,079/share on March 31, 2024, this investment has already delivered a cumulative gain of about $1.38 billion (before carrying costs). This purchase was very creative and opportunistic and has become in three short years one of Fairfax's best investments ever.

11.) <u>In Dec 2021, reduced the average duration of its $37 billion bond portfolio to 1.2 years</u> (as interest rates bottomed). This action saved the company billions in bond losses – it protected the company's balance sheet. In turn, this has allowed the insurance subs to be aggressive in growing their top line in the hard market.

12.) <u>In Q4 2023, increased the average duration of its $45 billion bond portfolio to more than 3 years</u> (as interest rates were peaking). This locks in record interest income, currently running at about $2 billion annually, for the next 3 or 4 years.

The string of decisions executed by the fixed income team over the past 24 months were brilliant and have delivered billions in value to Fairfax's shareholders with much more to come.

13.) In 2020 and 2023, expanded partnership with Kennedy Wilson. Phase 1, in 2020, was the establishment of a $3 billion real estate debt platform. Phase 2, in 2023, was the purchase of $2 billion of PacWest loans yielding a fixed rate to maturity of 10%. Fairfax, through long term partner Kennedy Wilson, took advantage of a temporary market dislocation.

14.) In 2022, sold Resolute Forest Products for $626 million (plus $183 million CVR) at the top of the lumber cycle. Fairfax opportunistically sold at a premium price (at the top of the lumber cycle) what had been one their large chronically underperforming equity holdings. This sale also improved the overall quality of the remaining basket of equity holdings.

15.) In 2023, sold Ambridge Partners for $379 million, delivering a $259 million pre-tax investment gain.

Dividend: In January 2024, Fairfax increased their annual dividend 50% to $15/share. It had been $10/share going all the way back to 2011.

Share buybacks: Effective shares outstanding have decreased 17.1% over the past six years from 27.8 million in 2017 to an estimated 23.0 million in 2023, an average decline of 2.9% per year.

16.) in 2021, re-purchased 2 million shares at $500/share. This was 7.6% of shares outstanding at the time.

On March 31, 2023, Fairfax's share price closed at $1,079. Fairfax's significant share purchases the past 6 years were done at prices well below intrinsic value - which makes them very beneficial for the company and shareholders. This has been another financial home run.

The list above captures only the largest capital allocation decisions made by Fairfax in recent years. We could easily add another 15 smaller examples of transactions that are also proving to be of a material benefit to Fairfax.

For a comprehensive list of many of Fairfax's capital allocation decisions going back to 2010 (sorted by year) go to the Appendix of this document.

The importance of properly sizing your bet

A lesson from Stan Druckenmiller: position sizes really matter
- https://moneyweek.com/investments/investment-strategy/605020/stan-druckenmiller-position-size-really-matters

"Sizing is 70% to 80% of the equation. Part of the equation is seeing the investment, part of the investment is seeing myself in a good trading rhythm. **It's not whether you're right or wrong, it's how much you make when you're right and how much you lose when you're wrong**," says Druckenmiller.

Position size matters. A lot. If you don't believe Druckenmiller, just ask Buffett.

Now take a close look at the 16 examples I cited above. What jumps out? The size of the gain from each of the decisions. **My math says 9 delivered a $1 billion or more gain to Fairfax and its shareholders over time**. In recent years, Fairfax has been not only making very good decisions - it has been sizing them exceptionally well. The benefits to the company and shareholders have been massive - with much more to come.

Fairfax has a current market cap $26.5 billion. A $1 billion gain is a needle mover for the company. A bunch of them stacked one on top of the other? That is called 'escape velocity' for operating earnings. More on this point later in the post.

<u>Asset sales</u>

Asset sales is one part of capital allocation that separates Fairfax from its peers like Berkshire Hathaway and Markel. In selling an asset, Fairfax is essentially trading a stream of future cash flows for a lump sum today.

<u>Why should a company sell an asset?</u>

Sometimes another company - who is willing to pay up - values an asset at a much higher value than you do. The sale of the pet insurance business is a great example of this.

There also can be important strategic reasons to sell an asset. For instance, if a sale allows the company to better focus on other parts of its business (management time and capital), selling an asset can lead to improved financial results. Selling APR to Atlas is perhaps a good example of this. Selling lower quality assets is also a good way to improve the overall quality of the remaining holdings. Selling Riverstone UK (runoff) and Resolute Forest Products are perhaps two good examples of this.

Put simply, asset sales have been a very important part of Fairfax's capital allocation framework, realizing significant value for Fairfax and its shareholders over the years.

<u>Improving the quality of the two businesses - insurance and investments</u>

Over the past 6 years Fairfax has done a great job of improving the overall quality of both its insurance and equity holdings. Equities was where the heavy lifting needed to be done - and after years of effort Fairfax has made considerable progress with many underperforming holdings (sales, mergers, take-private, run-off). Other holdings, like Eurobank, always well managed, have been greatly assisted by external events (economic pivot in Greece).

Higher quality businesses are able to deliver larger and more stable earnings. And that is what we are starting to see. Analysts have been slow to recognize this change, which is one reason why their estimates were usually too low in 2023.

Is Fairfax's capital allocation record perfect?

No, of course not. No company is perfect on this front. I see two notable misses:

- Taking until late 2020 to exit the last short position (and not exiting earlier).
- Not finding a way to unload Blackberry during the WallStreetBets mania that caused the share price to spike for a very short period of time in 2021. Fairfax says they were unable to act due to being in a blackout period in place at the time.

Looking at everything they have done over the past five years, it is clear that Fairfax has been executing exceptionally well.

"In this business if you're good, you're right six times out of ten. You're never going to be right nine times out of ten." *Peter Lynch*

Looking at Fairfax's track record over the past five years, I would argue that the company has been right with their capital allocation decisions at a rate much higher than 6 out of 10.

In Druckenmiller parlance, Fairfax has been on a multi-year "hot streak". Or in Buffett parlance, Fairfax has been hitting the ball like Ted Williams for the past couple of seasons.

Has Fairfax simply been lucky?

Did Prem give the team at Fairfax a sip of 'liquid luck' back in 2018? Some luck likely has been involved. But I like this definition of luck:

"Luck is what happens when preparation meets opportunity." *Roman philosopher Seneca*

What have we learned?

Here are the words I would use to describe Fairfax's approach to capital allocation:

- Flexible - use the full suite of options available.
- Opportunistic - take advantage of dislocations/opportunities as they arise.
- Countercyclical - act contrary to prevailing investment trends.
- Speed - act quickly when necessary.
- Conviction (position sizing) - go big when risk/reward is highly compelling/asymmetrical.
- Creative - be open minded during the process.
- Long term focus – goal is to generate above-market returns. Accepting of volatility.
- Strategic - make the company stronger - both insurance and investments.
- Rational - capital goes to the best (risk adjusted) opportunities.
- Equally capable in executing across both insurance and investment businesses.

What has been the financial impact of Fairfax's capital allocation decisions?

Operating Income:

Let's start by looking at operating income given it is viewed by analysts as the most important part of an insurance company's total earnings. Operating income at Fairfax is the sum of three things: underwriting profit, interest and dividend income and share of profit of associates.

For the 5-year period from 2016-2020, operating income at Fairfax averaged $1 billion per year or $39/share. Compared to the 5-year averaged from 2016-2020:

- in 2021, operating income doubled to $1.8 billion or $77/share.
- in 2022, operating income tripled to $ 3.1 billion or $132/share.
- in 2023, operating income more than quadrupled to $4.4 billion or $193/share.

In 2024, operating income is estimated to be about $4.5 billion or $198/share. The estimate for operating income per share in 2024 ($198/share) is 5 times larger than the average from 2016-2020 ($39).

What is the reason for the spike higher? **The dramatic increase is due in large part to the exceptional capital allocation decisions made by the management team at Fairfax over the past 6 years.** Importantly, the gains in operating income are durable as they have been driven by improving fundamentals (not one-time items).

Fairfax - Operating Income									
March 31, 2024	**2016**	**2017**	**2018**	**2019**	**2020**	**2021**	**2022**	**2023**	**2024E**
Underwriting profit - ins & reins.	$576	-$642	$319	$395	$309	$801	$1,105	$1,522	$1,243
Interest & dividends	$555	$559	$784	$880	$769	$641	$962	$1,896	$2,230
Share of profit of associates	$24	$201	$221	$170	-$113	$402	$1,015	$1,022	$1,030
Operating income - ins & reins	**$1,155**	**$118**	**$1,323**	**$1,444**	**$965**	**$1,844**	**$3,082**	**$4,441**	**$4,503**
Per share	$50	$4	$49	$54	$37	$77	$132	$193	$198
Shares Outstanding Dec 31	23.1	27.75	27.2	26.8	26.2	23.9	23.3	23	22.7

Investment Gains:

The other important part of earnings is asset monetizations and investment gains. This lumpy part of earnings has historically been a strength for Fairfax - the pet insurance and RFP sales in 2022, and the Ambridge Partners sale in 2023, being three recent examples. We should expect Fairfax to continue to deliver solid (but lumpy) investment gains moving forward.

My current estimate has Fairfax on track to deliver record earnings of around $160/share in 2024.

Return On Equity:

For the 5-year period from 2016-2020, ROE averaged about 6.0% per year. For the period 2021-2024, ROE is tracking to average 17.1%. That is a significant improvement.

Fairfax									
March 31, 2024	2016	2017	2018	2019	2020	2021	2022	2023	2024E
Earnings Per Share	-$24	$67	$12	$73	$7	$129	$47	$187	$160
Dividend	$10	$10	$10	$10	$10	$10	$10	$10	$15
Year End Book Value Per Share	$367	$450	$432	$486	$478	$631	$658	$940	$1,085
Return On Equity (average)	-6.3%	16.3%	2.7%	15.9%	1.4%	23.3%	7.2%	22.0%	15.8%
						IFRS-17	$762		

Important: I have use 'average equity' to calculate ROE. Some P/C insurers (like WRB) use 'beginning year equity' in their calculation (which results in a slightly higher number).

Driven by strong capital allocation decisions, all important financial metrics at Fairfax have been materially improving in recent years. This strong performance looks set to continue in 2024.

How is the strategic positioning of Fairfax's businesses?

Insurance
- Significant expansion by acquisition 2015-2017 - build out of global platform is complete.
- Significant expansion by organic growth 2019-2023 - hard market
- Ongoing bolt-on acquisitions, like Singapore Re, has further strengthened the business.
- Ongoing buy-out of minority partners, like Eurolife in 2021 and Allied World in 2022, and majority partner KIPCO (GIG) in 2023, has further strengthened the business.
- The quality of the insurance businesses continues to improve.
- The business is delivering record net premiums written and record underwriting profit.

Investments - fixed income:
- 2021: shortened duration of portfolio to 1.2 years and shifted to primarily government bonds in late 2021, to protect the balance sheet.
- 2023: extended duration to + 3 years to lock in much higher rates.
- 2023: capitalized on dislocations in financial markets to lock in even higher rates - with KW, purchased $2 billion in PacWest real estate loans yielding a total return of 10%.
- The positioning of fixed income portfolio has rarely looked better.
- The portfolio is delivering record interest and dividend income.

Investments – equities:
- Total return swaps, giving exposure to 1.96 million Fairfax shares, looks well positioned.
- Eurobank - balance sheet is fixed, earnings are strong. Greece is expected to be a top performing economy in Europe in the coming years. Purchase of Hellenic Bank will be a catalyst in 2024.
- Poseidon / Atlas - is currently in rapid growth mode.
- Investments in India (Fairfax India/BIAL etc) look well positioned given India is expected to be the fastest growing world economy in the coming decade.
- The rest of the company's portfolio looks well positioned.
- The quality/prospects of the portfolio of equities Fairfax owns have rarely looked better.
- The portfolio is delivering record share of profit of associates and sold investment gains.

Summary: The strategic positioning of each of Fairfax's three economic engines (insurance, fixed income and equities) has been steadily improving for the past five years.

Conclusion

Fairfax has a strong management team.

- They have been executing exceptionally well over the past 6 years.
- They are now delivering record financial results.
- Both businesses - insurance and investments - appear very well positioned.

Fairfax is delivering on the dual core objectives from capital allocation:

1. Deliver good/great returns on capital deployed
2. Improve the quality of each of the businesses (insurance and investments) over time

As a result, I think we can fairly conclude that the management team at Fairfax have demonstrable best-in-class capital allocation skills, and not just within their peer group in P/C insurance.

And with the company producing record operating earnings (and an estimate of around $4 billion in earnings) this best-in-class team is going to get the opportunity to deploy billions each year moving forward into new opportunities.

Record, sustainable and growing earnings + exceptional capital allocation + compounding + time = exponential growth

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Fairfax is trading today at a P/BV of about 1.1 (using my estimate of book value at March 31, 2024). That is a very low valuation - it suggests Fairfax is a poorly run P/C insurer with poor prospects.

If Fairfax is best-in-class at capital allocation, how can it also be poorly run with poor prospects? The answer is simple - it can't be both at the same time.

If Fairfax is above average at capital allocation, then future earnings growth should be solid. This will lead to an above average ROE.

As Mr Market comes to understand Fairfax better - and that the company is an above average P/C insurer, then we should see multiple expansion.

The trifecta for a stock: Growing earnings + growing multiple + lower share count = much higher share price.

'Time is the friend of the wonderful business.' Warren Buffett

Insurance - Is Fairfax a Growth Company?

Updated April 7, 2024

Is Fairfax a growth company? I realize that sounds like a dumb question to ask. I mean this is Fairfax after all. But hey, just for fun, what do the numbers tell us?

2014-2023: 9-Year Growth Numbers

Fairfax has grown net premiums written from $6.1 billion in 2014 to $22.9 billion in 2023, which is a total increase of 274%. That is a CAGR of 15.8% over the past nine years.

2024

In 2024, my current estimate has net premiums written increasing to $25.6 billion, for year-over-year growth of 12%. Growth will be split between organic (hard market) and the GIG acquisition.

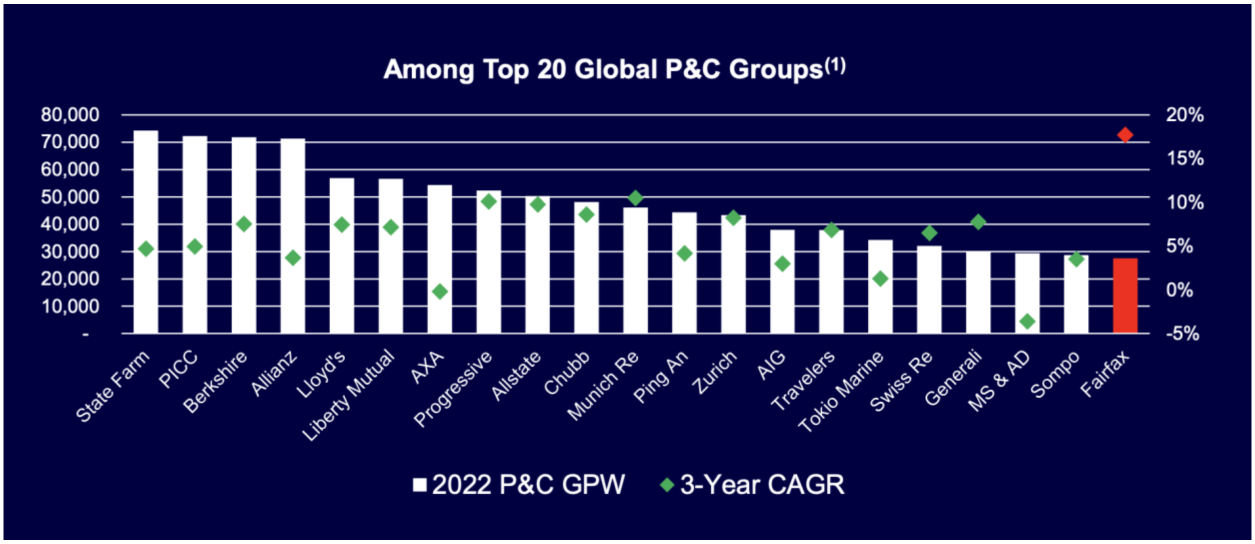
Over the 10 year period (2014-2024) this would result in a total increase in net premiums written of $19.5 billion or 318%, which is a CAGR of 15.4%. For a decade? Wow!

That performance is pretty impressive.

Fairfax: Growth of Net Premiums
Updated: April 7, 2024

	Net Premiums Written			Shares
31-Dec	**$b**	**%**	**/ share**	**m**
2014	$6.1		$289	21.2
2015	$7.5	23%	$339	22.2
2016	$8.1	8%	$350	23.1
2017	$10.0	23%	$359	27.8
2018	$12.0	20%	$442	27.2
2019	$13.3	10%	$495	26.8
2020	$14.7	11%	$562	26.2
2021	$17.8	21%	$745	23.9
2022	$22.3	25%	$957	23.3
2023	$22.9	3%	$996	23.0
2014-23	**$16.8**		**$707**	**1.8**
%	**274%**		**245%**	**8%**
CAGR	**15.8%**		**14.7%**	**0.9%**
2024E	$25.6	12%	$1,128	22.7
2014-24	**$19.5**		**$839.1**	**1.5**
%	**318%**		**291%**	**7%**
CAGR	**15.4%**		**14.6%**	**0.7%**

Guess how many large cap Canadian companies have grown their top line by 15.4% for a decade straight? Not many. Apparently not many P/C insurance companies either. Like a goat going up a mountain, Fairfax has been nimbly and quickly climbing the rankings of the largest global P/C insurers. In 2021 they were top-25 and in 2022 they quietly moved up into the #21 position.



Source: *Fairfax AGM April 2023 from S&P Global Market Intelligence*

So, let's ask that question again… Is Fairfax a growth company? Yup.

WOW! A Canadian company that is competing against the best the world has to offer… and not just playing the game (that participation award thing we love here in Canada) but actually winning? That is crazy. Canada must be so proud! Let's invite Prem to Ottawa, hold a parade and celebrate!

Except… ummm… few people in Canada seems to know that Fairfax exists let alone that it has been growing like a weed. It looks like most investors are also in the same boat because how does Mr. Market reward a fast-grower's share price?

Fairfax (US$)	**Mar 31, 2024**	
Share Price	$1,079	
2023 Earnings	$187	
P/E	5.8	
	Dec 31, 2023	**Dec 31, 2022**
Book Value	$940	$762
P/BV	1.15	
ROE (average equity)	22%	

Fairfax's stock price looks cheap. Makes no sense to me. But, hey, we all know Mr. Market is always right. Right? Except of course when Mr. Market is completely wrong. (That is called a fat pitch by some country bumpkin who lives in Omaha. But hey, that is a story for another day.)

Today, let's dig into what happened at Fairfax over the past eight years to drive all that top line growth. I will also explain why I am optimistic over the near term, even though the hard market looks like it might be slowing.

The 15.8% CAGR in net premiums written that Fairfax has delivered over the past 9 years has happened in two pretty distinct phases. Then I will take a stab at what might come next:

- Phase 1: Acquisitions – international expansion (2015-2017)
- Phase 2: Organic - hard market (2019-2023)
- Phase 3: Take-out of minority partners (2022-2025)

As one would expect, there is some overlap with these phases. So, let's peel back the onion a little bit and review what happened in each phase. What did Fairfax do? What was the cost? Was it good for shareholders? By digging a little deeper, we can learn more about Fairfax and better evaluate the performance of the management team.

Phase 1: Acquisitions – international expansion (2015 to 2017)

Fairfax has used acquisitions to help fuel its growth through its entire existence and unlike many P/C insurers, Fairfax has long had an international presence. Over a three year period, from 2015-2017, Fairfax made six separate acquisitions that cost a total of $7.5 billion.

Acquisitions and Minority Partners

		Total	Fairfax		Partners		
		$	$	own	$	own	comment
2015	Brit (Lloyds of London)	$1,657	$1,141	70%	$516	30%	OMERS
	Eurolife (Greece)	$361	$181	40%	$180	40%	20% Eurobank
2016	AMAG (Indonesia)	$179	$170	100%	$0		
	AIG (Lat AM & Cent Eur)	$240	$240	100%	$0		
	Zurich South Africa	$128	$128	100%	$0		renamed Bryte
2017	Allied World	$4,900	$3,340	67.5%	$1,560	32.5%	OMERS, AimCo
	Total	**$7,465**	**$5,200**		**$2,256**		

How did Fairfax pay for the acquisitions? At the time, Fairfax was short on cash as the investment side of the business was underperforming (losses from equity hedges… yes, sorry to keep picking that scab). Fairfax funded the purchases through:

- stock issuance: $3.34 billion (7.225 million shares at $462/share)
- minority partners: $2.256 billion (see above)
- asset sales: Bank of Ireland, ICICI Lombard, First Capital, Ridley

The deal with the minority partners is interesting:

> "In the case of both Brit and Eurolife, we expect to be able to acquire the interests back within the five years after closing, after providing OMERS with an acceptable return. The team at OMERS has been a pleasure to deal with." *Prem Watsa - Fairfax 2015AR*

Allied World is structured similarly. Finding a temporary partner was a very creative funding solution. I think the partners make an annual rate of return (of around 8% per year?) and Fairfax is able to buy back the stakes when they have the cash and at an acceptable price, negotiated when the deal is struck, I believe.

Timing?

In hindsight, 2015-2017 was a good time to buy insurance companies because they were valued at reasonable prices and it was right before the start of the hard market. The timing of the purchases was likely not a fluke. Fairfax saw value and was being opportunistic.

How much did Fairfax grow over the 4-year period from 2014-2018? Net premiums written increased from $6.1 billion in 2014 to $12.0 billion in 2018, for total growth of $5.9 billion or 96% over 4 years. Yes, the share count did increase quite a bit so growth per share was lower at 53% (more on this later).

Fairfax: Growth of Net Premiums
Updated: Oct 12, 2023

	Net Premiums Written			Shares
31-Dec	$bn	%	/ share	mn
2014	$6.1		$289	21.2
2015	$7.5	23%	$339	22.2
2016	$8.1	8%	$350	23.1
2017	$10.0	23%	$359	27.8
2018	$12.0	20%	$442	27.2
2014-18	**$5.9**		**$153**	**6.0**
%	**96%**		**53%**	**28%**

Growth by acquisition can be good but it carries risks. Did you overpay? Are there hidden issues (such as poor reserving)? Are there integration/culture issues? What is the best way for an insurance company to grow? The simple answer is a hard market and that is what started in Q4 of 2019.

Phase 2: Organic - hard market (2019-2023)

Hard markets for P/C insurers are rare. The last one was in 2001-2004. What makes a hard market so good? The opportunity to charge higher premiums and to apply more stringent underwriting (more favourable terms and conditions on policies). For well-run insurers like Fairfax, a hard market is like getting a gift from the insurance gods.

Fairfax was very well positioned for the hard market that started in late 2019. And they have been taking full advantage of it for the past 5 years.

How much did Fairfax grow over the 5-year period from 2018-2023? Net premiums written increased from $12.0 billion in 2018 to $22.9 billion in 2023, for total growth of 91% over five years. However, during this period the share count decreased by 15% so growth per share was higher at 125%. That is rocket-ship-emoji type organic growth over five years.

Fairfax: Growth of Net Premiums				
Updated: April 7, 2024				
	Net Premiums Written			**Shares**
31-Dec	**$bn**	**%**	**/ share**	**mn**
2018	$12.0		$442	27.2
2019	$13.3	10%	$495	26.8
2020	$14.7	11%	$562	26.2
2021	$17.8	21%	$745	23.9
2022	$22.3	25%	$957	23.3
2023	$22.9	3%	$996	23.0
2018-23	**$10.9**		**$554**	**-4.2**
%	**91%**		**125%**	**-15%**

The hard market is the best way for an insurance company to grow but they do not last forever. And it looks like the current hard market is slowing. Does that mean the growth story is over? No. Because Fairfax has set the table nicely for what will likely drive the next phase of growth for the company: the buying out of their minority partners.

<u>Phase 3: Take-out of minority partners (2022-2025)</u>

Fairfax started executing this strategy over the past couple of years but it picked up steam in 2022 and 2023 with the Allied World and GIG transactions.

- 2018 & 2021 Eurolife
    - Increased ownership from 40% to 50% and then to 80%. The last 30% was purchased from OMERS for $143 million.
- 2021 Singapore Re
    - Paid $103 million to increase ownership from 28.1% to 96% (now 100%)
- 2022 Allied World
    - Paid $733 million to increased ownership from 70.9% to 82.9%
    - In Q2 of 2023, Fairfax spent $31 million to boost their stake in Allied to 82.4%.
- 2023 Gulf Insurance Group
    - Fairfax took out the majority partner, KIPCO, with this purchase.
    - Fairfax increased their stake from 43.7% to 90%.
    - Paid $740 million ('fair value aggregate valuation').

Why could we see this strategy pick up steam in the coming years? The answer is that Fairfax is now generating an estimated $4 billion per year in earnings. What will Fairfax do with this Smaug-like mountain of gold that will likely be piling up? Especially when the hard market ends in another year or two and the insurance subs do not need as much capital to fund their growth?

Moving forward I think it is likely that Fairfax will to continue buy out the minority partners in their insurance businesses. These transactions are low risk (Fairfax knows the assets) and they offer a solid rate of return (whatever was being paid to minority partners). Taking out the minority partners also simplifies Fairfax's structure and makes the company easier to understand.

Is buying out a minority partner like a share buyback?

Some on this board have stated that buying out minority partners is kind of like doing a share buyback. Because shareholders get an even larger piece of Fairfax's growing earnings.

Conclusion

After all this, what did we learn? The management team at Fairfax has been masterful at taking advantage of the changing environment - both the external (in the insurance market) and internal (at Fairfax). Their planning, creativity and execution over the last eight years has built Fairfax into a global insurance giant that looks very well positioned today for continued growth.

What does this mean for investors?

Growth investing is defined as identifying and investing in companies with above average growth prospects compared to the industry/peers. Over time, higher growth leads to higher earnings which usually leads to a higher stock price. For growth investing to work the company needs to be successful - does the growth and higher profitability actually happen?

What does this have to do with Fairfax?

Well, the growth has already happened at Fairfax. And the increase in profitability is starting to kick in. And little of this appears to be reflected in the stock price - yet. Investors in Fairfax are benefitting today from years of growth that has already happened (top line) and they appear to be getting much of that growth (increasing profitability) for free. That, of course, sounds preposterous. But it appears to be true.

Fairfax is, after all, a growth company - one that has been hiding in plain sight.

'One more thing:' Fairfax owns a significant amount of Digit. Who is Digit? It is one of the fastest growing general insurance companies in India. But that is a story for another day.

Fairfax and the Transition from Good to Great: The Flywheel Effect

Updated April 7, 2024

Fairfax's stock is currently trading at a PE of 5.8 (to trailing 2023 earnings).

Fairfax (US$)	Mar 31, 2024
Share Price	$1,079
2023 Earnings	$187
P/E	5.8

Of course, it is not normal for a stock to trade at a PE of 5.8. The PE multiple for the S&P500 is currently about 20.

Fairfax's PE of 5.8 screams one of two things is clearly wrong:

- the price of the stock is way too low.
- earnings are way too high (and not 'durable')

<u>Let's take a look the stock price first</u>.

Fairfax has been one of the best performing stocks over the past 3.25 years. From Dec 31, 2020 to Mar 31, 2024, Fairfax is up 216% while the S&P500 is up 40%. Fairfax has outperformed the S&P500 by 176%. That is stellar outperformance.

Fairfax (US$)	Share Price	YOY change			S&P500	YOY change	
Dec 31, 2020	$341		increase		3,756		increase
Dec 31, 2021	$492	44%	over		4,766	27%	over
Dec 31, 2022	$594	21%	past 39		3,840	-19%	past 39
Dec 31, 2023	$921	55%	months		4,770	24%	months
Mar 31, 2024	$1,079	17%	216%		5,254	10%	40%

After a run like that, Fairfax's stock price must now be fairly valued. Right? Perhaps. But before we draw and conclusions, let's continue with our analysis.

<u>Let's take a look at earnings estimates</u>.

Below are my current earnings estimates for Fairfax for the next two years:

- 2024 = $160/share
- 2025 = $165/share

My forecast is for earnings to average about $162.50/share for each of the next 3 years. Clearly, my estimates must be too way high. Right? I actually think they might prove to be conservative. Why? Because most of the forecasts I have done for Fairfax for the past 3 years have proven, in hindsight, to be too conservative and usually by a lot.

Why have my estimates been too low? Because I have been consistently underestimating the management team at Fairfax and the earnings power of the collection of assets they have today. So, I trust my earnings estimates looking out the next two years.

Then what explains Fairfax's current very low PE of 5.8?

Despite a 216% gain over the past 3.25 years, the share price of Fairfax looks like it is still dirt cheap. Yes, that probably sounds like crazy talk.

How can a 'still dirt cheap' stock price be explained?

Operating earnings are the holy grail for insurance companies because it is made up primarily of fairly predictable items. And these items tend to be durable. Let's focus on this bucket of earnings at Fairfax and see what we can learn.

The average for total operating earnings at Fairfax from 2016 to 2020 was $1 billion per year ($39/share). But this dramatically changed beginning in 2021. Compared to the 2016-2020 average:

- In 2021, operating earnings doubled to $1.8 billion or $77/share
- In 2022, operating earnings tripled to $3.1 billion or $132/share
- In 2023, operating earnings more than quadrupled to $4.4 billion or $193/share

Over the past 3 years, the increase in operating earnings at Fairfax has been like a goat climbing straight up the steep side of a mountain.

Fairfax - Operating Income									
March 31, 2024	**2016**	**2017**	**2018**	**2019**	**2020**	**2021**	**2022**	**2023**	**2024E**
Underwriting profit - ins & reins.	$576	-$642	$319	$395	$309	$801	$1,105	$1,522	$1,243
Interest & dividends	$555	$559	$784	$880	$769	$641	$962	$1,896	$2,230
Share of profit of associates	$24	$201	$221	$170	-$113	$402	$1,015	$1,022	$1,030
Operating income - ins & reins	**$1,155**	**$118**	**$1,323**	**$1,444**	**$965**	**$1,844**	**$3,082**	**$4,441**	**$4,503**
Per share	$50	$4	$49	$54	$37	$77	$132	$193	$198
Shares Outstanding Dec 31	23.1	27.75	27.2	26.8	26.2	23.9	23.3	23	22.7

Let's now do some historical comparisons to see what we can learn.

From 2016 to 2020, Fairfax's stock price averaged about $500/share (I am ignoring the covid drop in 2020). Over this same 5-year period, operating earnings at Fairfax averaged about $1 billion per year ($39/share). Investors over this 5 year period thought $1 billion in operating earnings at Fairfax was worth a stock price of about $500. Back then, Fairfax's stock was considered to be fairly valued.

In 2023, operating earnings at Fairfax finished at $4.4 billion ($193/share). Operating earnings for 2023 are up 344% compared to the old 5-year baseline trend from 2016-2020, or 395% on a per share basis (the share count has come down over the past 5 years).

Fairfax's stock price was $1,079 at March 31, 2024. Fairfax's stock price is up only 116% compared to the 5-year trend from 2016-2020.

So operating earnings per share at Fairfax have increased a staggering 395% over the 2016-2020 trend while the share price has increased only 116%. I think we just learned something useful. The increase in Fairfax's stock price has not kept up with the increase in operating earnings. And 'not kept up' is a big understatement.

<u>What is Mr. Market missing?</u>

Mr. Market clearly is not understanding the new trajectory for operating earnings at Fairfax.

This is likely because Mr. Market is still looking at Fairfax's financial performance through the rear view mirror - focussing primarily on past reported results. That approach makes sense for most companies. But it makes no sense for Fairfax today. Because it completely misses (ignores) all the significant positive changes that have been happening at Fairfax over the past 5 years - the benefits of which are only just now fully flowing through to reported results.

The good news is Mr. Market will eventually figure things out at Fairfax. Earnings are the key. And as Fairfax keeps reporting stellar results quarter after quarter, Mr. Market will price Fairfax's shares more appropriately.

<u>What is causing the massive increase in operating earnings?</u>

What we are seeing today, with record operating earnings at Fairfax, is the cumulative effect of slow, organic (internal) change that has been happening at Fairfax for many years - a process of continuous improvement. It is the result of the conscious choices and actions being taken at all levels of the organization - senior management, the insurance operating companies, the investment team at Hamblin Watsa and the CEOs of the various equity holdings. All parts of the organization are working in a disciplined way towards the same end purpose - the consistent delivery of solid results leading to the improvement of the long term performance of the company. It is the slow methodical process of doing what needs to be done.

For Fairfax the process also involved some soul searching - there were lessons that needed to be learned. Fairfax stopped doing the things that were not working (like the equity hedges and short positions). It got better with its new equity investments.

The improving operating earnings are also not due primarily to circumstance - active management (taking advantage of circumstance) is an important part of Fairfax's business model.

The record operating earnings we are seeing at Fairfax today is simply the end result of years of good decisions and hard work.

What is the new baseline for operating earnings at Fairfax today?

The level of operating earnings at Fairfax have likely reached an inflection point - a breakthrough of sorts - given their size. Significant sums are now being reinvested every year (billions). The seeds that are being planted in both insurance and investments will grow new streams of operating earnings for Fairfax in the coming years. Compounding and time will work its magic. Fairfax looks like it is now in that virtuous circle where success begets more success.

My estimate for operating earnings for 2025 is $4.5 billion and I think that is a reasonable number to use a new baseline for Fairfax moving forward. Why? Because all the inputs I use are reasonable and (I think) mildly conservative.

How durable is $4.5 billion in operating earnings?

My guess is it is quite durable. At least as durable as operating earnings at other P/C insurance companies like WR Berkley, Markel or Chubb. Why wouldn't they be? In fact, the management team at Fairfax has been best-in-class in terms of overall management of the business in recent years - this suggests that we should have more confidence in Fairfax's future results than that for peers. I know, that is a very non-consensus view. But it is where logic takes me.

As I like to say, the once ugly caterpillar called Fairfax has magically transformed itself into a beautiful butterfly. What thing happened to cause the transformation? There was no one thing. It was a bunch of things. From the butterfly's point of view, what happened was perfectly natural. Only to the outsider does it look like magic.

Jim Collins, in his book *Good to Great*, has a concept called the '*flywheel effect*' that describes very well what has been happening 'under the hood' at Fairfax for the past 5 or 6 years that has got the company to where it is today.

"The Flywheel effect is a concept developed in the book Good to Great. No matter how dramatic the end result, good-to-great transformations never happen in one fell swoop. In building a great company, there is no single defining action, no grand program, no one killer innovation, no solitary lucky break, no miracle moment. Rather, the process resembles relentlessly pushing a giant, heavy flywheel, turn upon turn, building momentum until a point of breakthrough, and beyond."

https://www.jimcollins.com/concepts/the-flywheel.html

What are some of the decisions/actions made by Fairfax in recent years that have caused the Fairfax 'flywheel' to pick up more and more speed? To provide some context, we are going to separate the decisions/actions into Fairfax's three economic engines:

- insurance
- investments - fixed income
- investments - equities/derivatives

Each on its own is driving higher earnings for Fairfax. Together, they help illustrate why Fairfax is delivering record operating earnings - and why the Fairfax flywheel has now likely reached 'breakthrough' speed.

Economic engine 1: insurance

- Turn 1: 2015-2017: rapid growth - driven by international expansion by acquisition
- Turn 2: 2017: strategic pivot in India - sold ICICI Lombard for a significant gain ($950 million) and seeded Digit with an investment of $154 million that is now worth $2.265 billion.
- Turn 3: 2019 to today: rapid organic growth - driven by hard market.
- Turn 4: 2022: increased ownership in Allied World from 70.9 to 82.9%
- Turn 5: 2023: increasing ownership in Gulf Insurance Group from 44% to 90%. Strategic; control; secures Fairfax's position in MENA.
- Turn 6: ongoing: methodically improving quality of the total insurance businesses. Resulting in improving CR.

Net premiums written have increased from $8.1 million in 2016 to $22.9 billion in 2023, an increase of 183%. At the same time, the combined ratio has improved from an average of 98.2% from 2016-2020 to an average of 94.3% from 2021-2023. Much higher net premiums written and a lower CR has resulted in much higher (record) underwriting profit. Underwriting profit averaged $191 million per year from 2016-2020. It was $801 million in 2021, $1.1 billion in 2022 and $1.5 billion in 2023. This increase looks sustainable (with some volatility in both directions).

Economic engine 2: investments - fixed income

- Turn 7: December 2021: average duration of fixed income portfolio was reduced to 1.2 years. In 2021, sold $5.2bn in corporate bonds at a yield of 1% for a realized gain of $253 million (most were purchased in March/April 2020). Avoided billion in unrealized losses on $40 billion fixed income portfolio as interest rates spiked higher in 2022 and 2023. This protected the balance sheet.
- Turn 8: Q4 2023: average duration of fixed income portfolio was extended to more than 3 years. This likely locks in record interest and dividend income of more than $2 billion for the next three years.
- Turn 9: 2020 and 2023: real estate debt platform partnership established with Kennedy Wilson. $4 billion portfolio is delivering an average return of about 9% total = $360 million, mostly in interest income.

Driven by the significant increase in the insurance business, the size of the fixed income portfolio at Fairfax has more than doubled in size from $20.3 billion in 2016 to $45 billion in 2023. From 2016-2022, the average yield of the fixed income portfolio was 2.6% and today the average yield is about 4.4%. As a result of the two doubles (portfolio size and rate of return), interest income is spiking higher. Interest and dividend income averaged $709 million per year from 2016-2021. It was $962 million in 2022 and $1.9 billion in 2023 and is forecast to come it at $2.2 billion in 2024.

Economic engine 3: investments - equities / derivatives

- Turn 10: 2016: ending the 'equity hedge' in late 2016.
- Turn 11: 2020: closing out the final short position in late 2020

These two programs cost Fairfax an average of $494 million per year from 2010-2020. Ending these two programs eliminated what was essentially a $494 million annual expense for the company. Fairfax has also said multiple times that they have learned their lesson and that they will no longer short indices or individual stocks.

- Turn 12: 2014-2017: poor equity purchases - Fairfax made a string of poor equity purchases from 2014-2017.
- Turn 13: 2018 to today: very good new equity purchases - Fairfax has been hitting the ball out of the park with their more recent new equity purchases.
- Turn 14: 2020-present: Fairfax also took advantage of the recent bear market in stocks by adding significantly to many of the equity holdings they already own.

Fairfax has done a great job over the last 5 years of fixing their poor equity purchases from 2014-2017. These holding were burning about $200 million per year in cash (losses/write downs/restructuring charges etc) and now they are all largely fixed and delivering solid returns for Fairfax shareholders. Eurobank is the shining star in this group. The new equity purchases from 2018 to today have been performing well. And Fairfax aggressively added to positions in equities they already owned - buying at bear market low prices.

Share of profit of associates at Fairfax averaged $151 million per year from 2016-2021. It was $1 billion in 2022 and another $1 billion in 2023. This number should grow nicely in the coming years (with some volatility in both directions).

The quality of Fairfax's total portfolio of equity holdings has likely never been better than it is today.

- Turn 15: late 2020/early 2021: purchase of total return swap giving Fairfax exposure to 1.96 million FFH shares at an average cost of $373/share. This one investment has delivered to Fairfax an investment gain of about $1.38 billion since inception to March 31, 2024 (before carrying costs).

Asset sales:

- Turn 16: 2020/2021: sold Riverstone UK (runoff business) for $1.3 billion (plus $230 million contingent value instrument).
- Turn 17: 2022: sale of pet insurance business delivered a $1 billion after-tax gift to Fairfax shareholders.
- Turn 18: 2022: sale of Resolute Forest Products for $626 million (plus $183 million CVR) at top of lumber cycle.
- Turn 19: 2023: sale of Ambridge Partners for $379 million (plus $100 million performance target) which delivered a $259 million pre-tax gain.

Asset sales (insurance and investments) have always been an important part of the capital allocation framework at Fairfax and have delivered significant value to shareholders over the years.

Stock buybacks:

- Turn 20: 2021: Dutch auction - Fairfax purchased 2 million shares at $500/share.
- Turn 21: 2018 to present - via NCIB, Fairfax has bought back about 2.6 million shares via the NCIB at about $474/share.

Share count at Fairfax peaked at 27.75 million in 2017. Since that time Fairfax has reduced effective shares outstanding by 4.75 million or 17.1%. Share count today is below where it was in 2016 - more than offsetting the dilution caused by the Allied World acquisition. As a result, shareholders today enjoy the full benefit (on a per share basis) of the significant growth Fairfax has achieved since 2016. As well, all 4.75 million shares were repurchased at a very attractive average price of around $484.

Conclusion:

As you can see from the list above there is no one thing (action, event, luck) that is driving record operating earnings at Fairfax. Rather, it is the cumulation of many, many things that have happened over the past 5 or 6 years. But it is only now that the impact of these many actions is becoming fully visible to outsiders - because now they are together 'all of a sudden' showing up in record operating earnings. The flywheel has achieved breakthrough. And Fairfax as a company has made the leap from good to great.

Is Fairfax's stock fairly valued at a PE of 5.8 (to 2023 trailing earnings)? You decide.

The Benefits of active management:

Above is a list of 21 actions taken by the management team at Fairfax in recent years. A significant number of the actions mentioned have on their own delivered $1 billion or more in value to Fairfax shareholders. Each on its own is an impressive accomplishment. But when you put them all together… well that is simply an amazing collection of accomplishments. And a big reason why I am confident Fairfax's new baseline for operating profit is likely around $4.5 billion per year. It clearly demonstrates the huge impact active management, when done well, can have on the intrinsic value of a company like Fairfax.

What Are Some of the Risks of Investing in Fairfax?

Updated April 7, 2024

The best source for information on the risks of investing in Fairfax is, of course, the company itself. Start with the 2022 Annual Report (page 188) where Fairfax reviews this topic in great detail.

https://www.fairfax.ca/wp-content/uploads/WEBSITE-Fairfax-Financial-2022-Annual-Report_v2.pdf

I have spilt lots of digital ink writing what I like about Fairfax. Does that mean I am ignoring the risks? No, of course not. In this post I'd like to flip the script and write about a few of the risks of investing in Fairfax.

For starters, there are the usual run-of-the-mill risks:

- Will this be another bad year for catastrophes?
- Is the hard market ending?
- Is a severe recession coming?

These risks are important but out of Fairfax's control. With this post, I want to discuss the risks that are more specific to Fairfax - and firmly in their control.

What are the risks of investing in Fairfax?

Below I list 6. Of course, there are more. But these are the 6 watchouts that come to mind for me.

1.) Can management be trusted?

"It takes 20 years to build a reputation and five minutes to ruin it. If you think about that, you'll do things differently." *Warren Buffett*

2010-2020 was largely a lost decade for Fairfax shareholders.

Fairfax shredded its reputation not in 5 minutes but over a 10 year period. For Fairfax shareholders, the period felt like a death by a thousand cuts.

What happened? The short answers: Bad decisions. Poor communication. Terrible business results. Not a great combination. Long-term shareholders capitulated in May of 2020, and the stock dropped to US$230. Yes, Covid was partly to blame. But only partly.

What is interesting is it appeared things had been improving at Fairfax since about 2018. For the past six years we have seen much better decisions. The communication from the CEO is better. The business results have markedly improved. And now we now have a record high stock price.

Does that mean we are in the clear? No. Trust can only be re-built with time. So, we will see.

PS: Trust is the core building block of a strong relationship. If Fairfax wants long-term shareholders, then they need to do their part – and be a trustworthy partner.

The next two risks fall under the 'capital allocation' bucket:

2.) Do they make another 'equity hedge' type decision?

This is the big one for me. This one decision cost Fairfax shareholders a total of $5.4 billion from 2010 to 2020 (a loss of $494 million per year on average - for 11 straight years). Most of the losses happened from 2010-2016. However, in one last slap to the face of investors, Fairfax delivered a final $529 million loss in 2020. (Yes, how could an 'equity hedge' lose that much money in the bear market of 2020?)

Fairfax has said many times over the past few years that the 'equity hedge' position was a mistake. Further, they have said they will no longer short individual stocks or market indices. This was the key driver of underperformance at Fairfax from 2010-2020. We know this specific mistake has been fixed and will not be repeated in the future.

But does Fairfax make another big bet that sets them back +5 years? I don't see one today. But my eyes are wide open.

3.) Do they make a string of bad equity purchases in the near future?

Fairfax's equity picks from 2014-2017 were mostly terrible. By my count Fairfax made ten different purchases during this period of time that performed poorly and resulted in the company booking various losses that totalled about $1.5 billion from 2015-2022, or an average of about $200 million per year. (See 'A Review of 2014-2017: Old Fairfax' in Chapter 8.)

The good news? It looks to me like something changed at Fairfax in about 2018. Their equity purchases from 2018 to today have been very good. As well, the equities purchased from 2014-2017 - that were under-performing - have largely been fixed and are now performing well. (See 'A Review of 2018-2022: New Fairfax' in Chapter 8.)

In this area, I am not concerned today. But I do monitor each of their larger equity purchases.

4.) Financial leverage: increase in net debt

Fairfax is comfortable using leverage to boost shareholder returns. Over the past 5 years net debt at Fairfax has increased 84% while common shareholders equity has increased 73%.

Fairfax		**December 31**		**Increase**	
	US$ bn	**2023**	**2018**	**$**	**%**
Net debt *		$6.1	$3.3	$2.8	84%
Common shareholders' equity		$21.6	$12.5	$9.1	73%

Net debt * - excludes the debt of consolidated non-insurance companies

I don't see Fairfax's current net debt level as a problem. I estimate earnings will be very good over the next few years which, if it happens, would increase shareholders' equity meaningfully. Net debt is something to monitor.

5.) Corporate governance

Fairfax is a family controlled company (not unlike other founder led companies). Prem has a 10% economic interest and a 43.9% voting interest. Two of Prem's children currently serve as directors.

When a company is performing well, the issue of family control tends not to matter. However, when the company is not performing well, the issue of family control can become a big issue. Minority shareholders have little recourse should they be unhappy with the decisions management is making.

This is what it is.

6.) Reserving at the insurance companies

Fairfax's business model has changed dramatically over the past 38 years. For the first 20 years, it was kind of like 'make a bunch of money investing float and lose a little on underwriting'. The insurance part of the business model is what has changed the most over the years. The model shifted to something like 'break even on underwriting'. And for the past 13 years the model appears to have shifted again to 'make money on underwriting'.

Andy Barnard was put into his leadership role of managing the insurance operations in 2011 and he has done a solid job of slowly improving the quality of the insurance operations. Fairfax has a solid track record over this period on the underwriting/reserving front. And we are now in a hard market where pricing has been increasing materially each year since 2019.

How good are Fairfax's insurance operations? I suspect they might be higher quality than most investors currently think. If I am right this would provide a nice tailwind to future earnings.

Reserving at Fairfax is usually brought up as an 'issue' from anonymous posters on social media. Of course, they do not provide any facts (perhaps links to 20 year-old articles when some issues existed at Fairfax). It reminds me a little of the search for the Sasquatch. Yes, this mythical creature could be real. But like Bigfoot, Fairfax would have to be exceptionally good at hiding things. So, keep your eyes peeled next time you go for a walk in the forest…

Prem Watsa

Updated April 7, 2024

<u>Who is Prem Watsa?</u>

Prem is the founder and controlling shareholder of Fairfax Financial. He founded Fairfax in 1985.

From 1985 to 2023, Fairfax has delivered compound annual growth of:

- Book value per share = 18.4%
- Share price (CAN$) = 16.9%

This 38-year track record likely puts Fairfax in the top 1% of companies in the TSX and S&P500. Investors in Fairfax are partnering with one of Canada's best-ever capital allocators.

<u>What is Prem's ownership position in Fairfax today?</u>

- 10.2% economic interest is valued at $2.53 billion (at $1,079/share at Mar 31, 2024).
- 43.9% voting interest.

Prem Watsa's Ownership of Fairfax Shares

10% econimic ownership
43.9% voting control

1,548,000	The Sixty Two Inv Co - multiple voting shares
50,620	The Sixty Two Investment Company
741,985	Prem Watsa Owns
2,100	Prem Watsa Controls
2,342,705	Total Shares Owned / Controlled by Prem
$2.53	Market value ($b) at $1,079 share price (Mar 31, 2024)
23,003,248	Common Stock Effectively Outstanding (Dec 31, 2023)
10.2%	Prem's economic ownership

<u>What does this mean?</u>

Prem is firmly in control of Fairfax.

And the majority of his net worth is in Fairfax. This ensures there is a strong alignment of interests between Prem and shareholders.

Two of his children serve on the board: Christine McLean and Ben Watsa.

How much does Prem get paid by Fairfax?

- Salary: C$600,000/year. This salary has stayed the same for decades.

- Stock-based compensation: unlike other executives at Fairfax, Prem does not earn any stock based compensation.

For companies of Fairfax's size this is a pretty unique (and extremely low) compensation package. Looking at it strictly from a compensation perspective, this is a smoking good deal for shareholders.

Prem Watsa and Warren Buffett (to address the elephant in the room)

Yes, Prem has a few things in common with Warren Buffett:

1. Founder and controlling shareholder
2. Use insurance and float as the vehicle to drive growth
3. Value investor with a long-term focus
4. Operating companies are decentralized and run by their presidents
5. Small head office – handles capital allocation
6. Exceptional long-term track record of building wealth for shareholders

However, there are very important differences. When it comes to investing, the styles of Fairfax and Berkshire are quite different:

1. Size matters: Berkshire is looking for elephants. Fairfax is much smaller so its opportunity set is much larger. Along the same line, Berkshire is looking to buy complete businesses while Fairfax is usually looking to partner with others.
2. Unlike Berkshire, international is a large and growing part of Fairfax – both for insurance and investments. When Digit (India insurance start-up) was looking for a partner in 2016-17 they went to Berkshire first – who said no. Fairfax said yes. And Berkshire's loss has become Fairfax's gain. Fairfax's $154 million investment in Digit is now worth around $2.3 billion.
3. Fairfax is not a buy-and-hold forever investor. Selling is an important part of their capital allocation framework. The best recent example is the sale of their pet insurance business in 2022 for $1.4 billion, which resulted in a $992 million after-tax gain.
4. Fairfax is more of a deep value investor, although around 2018 it looks to me like they made some adjustments, like putting more of a premium on strong management (one example).
5. Fairfax is comfortable investing in commodities. More than 10% of Fairfax's equity portfolio today is invested in a diverse group of commodity plays – oil and gas, steel, mining, royalties.
6. Stage of Life Cycle: Buffett appears focused today primarily on preservation of capital – listening to him talk about his responsibilities to long term shareholders, he sometimes sounds like he is managing a trust. Fairfax is much younger in its life stage as a company and looks to still be focused on driving total return for shareholders.
7. Dividend: Unlike Berkshire, Fairfax pays a dividend (increased to $15/share in 2024).

Prem Watsa and John Templeton

From an investing perspective, if I had to compare Prem's/Fairfax's style to someone, I would probably pick John Templeton. John Templeton was a shareholder in Fairfax and a mentor of Prem's (they were friends). Templeton's great-niece, Lauren Templeton, is a Director at Fairfax. At the AGM this year, Fairfax gave away a small book titled: 'John Templeton: Words of Wisdom.'

> Broken Leg Investing: Your Ultimate Guide to John Templeton Investing (by Tobias Meier)
>
> https://www.brokenleginvesting.com/ultimate-guide-john-templeton-investing/

Prem Backs Up the Truck in June of 2020 and Buys $149 Million in Fairfax Shares

In the Covid driven stock market panic, Fairfax shares bottomed out at $250 in May 2020. Of interest, book value bottomed out at $442/share at March 31, 2020. The share price dropped back to the $260 level in October 2020. Shares were trading at prices last seen in 2007! For long-term investors of Fairfax, these were the darkest of days. Some likely capitulated and sold their shares. In 2020, the sentiment indicator for Fairfax's stock was flashing 'extreme fear'.

On June 15, 2020, Prem announced he had purchased 482,600 shares of Fairfax at a total cost of $148.95 million or $308.64/share. Prem was sending a message that he thought Fairfax's stock was dirt cheap. Few people at the time were paying attention. Fortunately, a few members at the investment forum 'Corner of Berkshire and Fairfax' were paying attention and were buying shares.

With Fairfax shares closing on December 31, 2023 at $920.76, Prem has made a paper gain of $295 million or 198%. Prem is a value investor and he certainly nailed this purchase. The significant size of the purchase was surprising, given how much Fairfax stock he already owned.

> "Mr. Watsa commented as follows in connection with this purchase: "At our AGM and on our first quarter earnings release call, I said that our shares are 'ridiculously cheap'. That statement reflected my recognition that in the 35 years since Fairfax began, I have never seen Fairfax shares sell at a bigger discount to their intrinsic value than they have recently. I have now backed up my strong words by purchasing close to US$150 million of Fairfax shares in the market over the last few days, as I believe that this will be an excellent long term investment." *Fairfax News Release June 2020*
>
> https://www.fairfax.ca/press-releases/prem-watsa-acquires-additional-shares-of-fairfax-2020-06-15/

Some context on the size of Prem's purchase:

In 2016, JP Morgan's CEO Jamie Dimon made his now famous purchase of battered JPM shares. How much did he spend? $26.6 million. In 2020, Prem purchased of $149 million of Fairfax stock. Prem's purchase was almost six times the size of Dimon's purchase.

In February of 2024, Jamie Dimon announced that he sold 822,000 of JP Morgan shares for proceeds of $150 million. This would have netted Jamie a gain of $65 million on his purchase of shares in 2016.

Prem still holds all of his Fairfax shares. He is up about $372 million on his purchase (initiated in June 2020).

	Stock Price	Shares	Value US$	
Jamie Dimon Buys JPM Shares				
Feb 2016	$53.15	500,000	$26,575,000	
Feb 23, 2024	$182.48	500,000	$91,240,000	
Jamie's Gain to March 31, 2024			**$64,665,000**	**243%**
Prem Watsa Buys Fairfax Shares				
June 2020	$308.64	482,600	$148,949,664	
Mar 31, 2024	$1,079.04	482,600	$520,744,704	
Prem's Gain To March 31, 2024			**$371,795,040**	**250%**

Chapter 2: Earnings Estimates – 2024 & 2025

Earnings Estimates – An Introduction

> "What possible assurance do you have that (a stock you own) will go up in price? And if you are buying, how much should you pay? What you're asking here is what makes a company valuable, and why it will be more valuable tomorrow than it is today. There are many theories, but to me, it always comes down to earnings and assets. Especially earnings." *Peter Lynch - One Up On Wall Street*

Estimating earnings for a company like Fairfax is difficult:

- It is a non-traditional insurance company – with significant equity holdings.
- A great deal of (good) change has been going on 'under the hood' for the past 5 years.
- It has been under-earning for much of the past decade.

As a result, the historical numbers are pretty messed up. But this has been changing the past couple of years. The turnaround in operating earnings that started in 2021 gathered steam in 2022. And with 2023 results out, we now have three years of 'good' information. Importantly, historical results can now be used as an important input to estimate future results.

However, given Fairfax is a non-traditional insurance company, estimating future results still has a fair degree of complexity. Bottom line, there is no 'over the counter' model out there that can be used to estimate earnings for Fairfax. But that difficulty also creates opportunity for those who are prepared to put in the time and do the work. As a result, we have built our own model to estimate the future earnings for Fairfax.

<u>Overview of our earnings model</u>

The core 'building blocks' we use in our model are:

- Underwriting profit
- Interest and dividend income
- Share of profit of associates
- Investment gains
- Shares outstanding

These items are the 'big rocks' – the fundamental drivers of Fairfax's business. If we can get the 'big rocks' right then there is a good chance our earnings estimate will prove to be reasonably accurate.

In our model, each building block above has their own detailed Excel worksheet. All worksheets flow through to a summary worksheet and that is how we arrive at our earnings estimate.

The posts in this chapter will dive into most of the building blocks listed above.

What is the logic we use to build our forecasts?

- We start with historical numbers. We have them going back to 2016.
- Adjust historical numbers to reflect both 'old news' and 'new news:'
    - Internal - company specific announcements/news: reported results, purchases, sales, management commentary; also include news from larger equity holdings
    - External - competition, P/C industry: status of hard market, impact of large catastrophes, economic developments (path of interest rates, state of the economy)
- Incorporate any other needed/relevant assumptions.

Each 'building block' post in this chapter provides a fair amount of detail so the reader has a basic understanding of the logic used to arrive at the forecasted numbers.

How far out does my crystal ball go?

I try and be as fact based as possible. As a result, I only go out two years with my forecasts. There are simply too many moving parts to try and forecast three years or more into the future with any precision. The future path of the hard market in insurance? The level of catastrophes? The future path of the economy, interest rates and financial markets?

For estimating earnings further out (more than 2 years), the quality of the management team is likely the most important factor - especially for P/C insurance companies. Are they good? How good? If they are very good you can have a fairly high confidence level that they will continue to deliver solid results in year 3 and after - you just don't know the details - yet.

The biggest problem with my earnings estimates for Fairfax over the past 2 years is I have often been too conservative - too low. So, I have been getting a little more aggressive with my estimates. Are my current earnings estimates now too optimistic? I don't think so. But I remain open minded.

Forecasting is a very dynamic process

The information in this chapter is outdated as soon as it is published. This is because as time passes, we constantly get new information. This newer, more accurate (better) information will cause earnings estimates to change – sometimes materially. As a result, I am constantly updating my forecasts (often weekly). Sometimes the changes will be small; other times they will be big.

When I write new posts, I use my current earnings estimates. I do not update other older posts in the document. Therefore, when you read a post, it is important to pay attention to the date it was written. It provides you with important context - what I was thinking on that date.

Doing a quality job with our earnings estimates should help us when we explore the intrinsic value/valuation question more fully in Chapter 3.

Earnings Estimates – Two Year Summary for 2024 & 2025

March 10, 2024

Below is an update to my two-year earnings estimate for Fairfax. Please note, forecasts are a guess at a point in time. To state the obvious, things are constantly changing. As a result, my earnings forecasts quickly become outdated. These forecasts are intended solely for entertainment purposes – please keep this in mind.

Since my last update, Fairfax has released both Q4 earnings and their 2023 annual report. This allows us to finalize results the 2023 year and update our forecasts for 2024 and 2025.

Summary

My current estimate is Fairfax will earn about $160/share in 2024 and about $165/share in 2025. For reasons outlined further below, I think both of these estimates have been constructed using mildly conservative assumptions.

Fairfax Earnings Estimate			
March 10, 2024			
US$	**EPS**	**BV/sh**	**ROE**
2023	$187	$940	22.0%
2024E	$160	$1,085	15.8%
2025E	$165	$1,236	14.2%
3-Yr Avg	$171		17.3%
Fairfax's $15 dividend has been subtracted from BV/share.			

2024 & 2025 Forecast

A hard piece to forecast with Fairfax is capital allocation. Fairfax is currently generating a significant amount of earnings. But we don't know today how the future cash flows will be invested:

- Grow insurance (continuation of hard market)
- Buy out minority partners in insurance?
- Equities or fixed income?
- Buy back a meaningful amount of Fairfax stock?
- Other?

Looking at the last 5 years, the management team has done an outstanding job with capital allocation. My guess is they will continue to make good decisions (on balance) and this will benefit shareholders – likely providing a tailwind to my forecasts for 2024 and 2025.

Using Yahoo Finance as a guide, analysts are collectively estimating that Fairfax will earn about US$148/share (C$200) in 2024 and US$157/share (C$211) in 2025 (using $0.742 US$/C$ exchange rate). Why are analyst estimates below my forecast? From what I can see, most analysts are assigning little benefit to future earnings and Fairfax's proven capital allocation skills. Most analysts will include these benefits into their earnings estimates <u>only after Fairfax has announced something</u>.

I am assuming interest rates remain roughly at current levels (at March 10, 2024). Of course, this will likely not be the case. But given the duration of the fixed income portfolio is now closer to the duration of the insurance liabilities, changes in interest rates (up and down) might kind of balance out (in 'net gains/losses on investments' and 'effects of discounting and risk adjustment- IFRS 17')

Below is an 8-year snapshot for Fairfax. It communicates in a concise manner the dramatic transformation that has happened at the company, beginning around 2021. There has been a spike in operating income per share – it has increased from an average of $39/share over the 5-year period from 2016-2020, to $192/share in 2023. This much higher amount now looks like the new baseline for the company. For 2024, my estimate has operating income increasing to $197/share, which is a 400% increase from the average from 2016-2020. Normalized earnings at Fairfax have moved to a much higher level – and, importantly, this level looks sustainable.

	Fairfax Financial - Earnings Estimates for 2024 & 2025										
	Used Sources of net Earnings & Net Earnings by Reporting Segment										
	Updated: March 10, 2024	**2016**	**2017**	**2018**	**2019**	**2020**	**2021**	**2022**	**2023**	**2024 FY est**	**2025 FY est**
1.)	Underwriting profit - ins & reins.	$576	-$642	$319	$395	$309	$801	$1,105	$1,522	$1,243	$1,280
2.)	Interest & dividends	$555	$559	$784	$880	$769	$641	$962	$1,896	$2,230	$2,200
3.)	Share of profit of associates	$24	$201	$221	$170	-$113	$402	$1,015	$1,022	$1,030	$1,100
	Operating income - ins & reins	**$1,155**	**$118**	**$1,323**	**$1,444**	**$965**	**$1,844**	**$3,082**	**$4,441**	**$4,503**	**$4,580**
	Per share	**$50**	**$5**	**$48**	**$54**	**$37**	**$71**	**$131**	**$192**	**$197**	**$203**
4.)	Effects of discounting and risk adjustment (IFRS 17)								$210	$260	$200
5.)	Life ins. & run-off	-$185	-$207	-$243	-$264	-$208	-$309	-$167	-$348	-$250	-$250
6.)	Other (rev-exp) Non-insurance sub	$103	$262	$264	$104	-$139	$71	$61	$46	$150	$200
7.)	Interest expense	-$243	-$331	-$347	-$472	-$476	-$514	-$453	-$510	-$520	-$530
8.)	Corp overhead and other	-$181	-$275	-$329	-$272	-$328	-$409	-$297	-$430	-$435	-$440
9.)	Net gains (losses) on investments	-$1,204	$1,468	$253	$1,716	$313	$3,445	-$1,734	$1,950	$1,000	$925
	Loss on repurchase of LT debt	$0	-$29	-$59	-$24	$0	$0	$0	$0	$0	$0
10.)	Gain on sale/deconsol of ins sub	$0	$1,019	$0	$0	$117	$264	$1,220	$550	$300	$300
	Pre-tax income (loss)	**-$554**	**$2,023**	**$862**	**$2,233**	**$244**	**$4,392**	**$1,712**	**$5,908**	**$5,008**	**$4,985**
11.)	Income taxes	$160	-$408	-$44	-$262	-$207	-$726	-$425	-$813	-$952	-$947
	Net earnings	**-$395**	**$1,615**	**$818**	**$1,971**	**$37**	**$3,666**	**$1,287**	**$5,095**	**$4,056**	**$4,038**
12.)	Non-controlling interests	$118	-$126	$442	-$33	-$181	$266	$140	$713	$385	$303
	Net earnings attrib. to FFH shareh.	**-$513**	**$1,741**	**$376**	**$2,004**	**$218**	**$3,401**	**$1,147**	**$4,382**	**$3,671**	**$3,735**
	Per share	-$24.18	$66.74	$12.03	$72.80	$6.59	$129.33	$46.62	$186.87	$160.31	$165.27
13.)	Shares Outstanding (weight. avg)	23	25.4	27.5	26.9	26.4	25.95	23.6	23.18	22.9	22.6
	Shares Outstanding Dec 31	23.1	27.75	27.2	26.8	26.2	23.9	23.3	23.0	22.7	22.4
	Avg Tax Rate	n/a	20.2%	5.1%	11.7%	84.8%	16.5%	24.8%	13.8%	19.0%	19.0%
	Annual Dividend	$10	$10	$10	$10	$10	$10	$10	$10	$15	$15
	Year-End Book Value	$367	$450	$432	$486	$478	$631	$658	$940	$1,085	$1,236
	ROE (average equity)	-6.6%	16.3%	2.7%	15.9%	1.4%	23.3%	7.2%	22.0%	15.8%	14.2%
	1.) Does not include run-off and Life Insurance						IFRS-17	$762			

What are the key assumptions?

1.) underwriting profit: Estimated to come in at $1.24 billion in 2024.

- Net written premiums growth of 12% in 2024 and 3% in 2025. This is being driven by:
  - Continuation of the hard market, which we estimate will add $1 billion of NWP.
  - The Gulf Insurance Group (GIG) acquisition, which will add $1.7 billion of NWP.
- Combined ratio (CR) of 95% in both 2024 and 2025.
  - Catastrophe losses: 2024 will be a more normal year (higher than 2023).
    - Fairfax continues to modestly shrink their total catastrophe exposure.
  - Reserve releases: continuation of the positive trend observed in 2023.

2.) interest and dividend income: Estimated to increase to a record $2.2 billion in 2024 and 2025

- Interest and dividend income in Q4 2023 was $536.6 million; this provides a good baseline (starting point)
- GIG adds about $2.4 billion to the total investment portfolio in 2024. A tailwind.
- Eurobank will start paying a dividend in 2H 2024. A tailwind.
- Rate cuts by global central banks would be a headwind in 2H.

3.) Share of profit of associates: Estimated to increase to a record $1.03 billion in 2024.

- Earnings at Eurobank, Poseidon, Stelco and Fairfax India, in aggregate, should continue to grow nicely. EXCO (nat gas prices) could be a headwind.
- GIG will be a small headwind as it is now consolidated.

4.) Effects of discounting and risk adjustment (IFRS 17):

- The two key drivers for this bucket are the trend in net written premiums of the insurance business and changes in interest rates.
- Net written premiums growth of 12% in 2024 should be a tailwind.
- I am modelling for interest rates to remain flat.
- This bucket is among the most difficult to model – therefore, my confidence level in my estimates is low.

5.) Life insurance and runoff:

- This combination of businesses lost about $348 million in 2023.
- I expect earnings in 2024 to be a little better – a lower loss of $250 million - with life insurance being a modest tailwind.

6.) Other (revenue-expenses) - non-insurance subsidiaries:

- Recipe, Dexterra, AGT, Grivalia Hospitality, Boat Rocker, Farmers Edge etc.
- This combination of businesses earned $46 million in 2023.
- I expect earnings to be better in 2024, coming in at $150 million.
- This bucket is poised to grow nicely for Fairfax in the coming years. It could surprise to the upside. Yes, the results will be lumpy.

7.) Interest expense: At $520 million, a modest increase to prior year of $510 million.
8.) Corporate overhead and other: At $435 million, a modest increase to prior year of $430 million.

9.) Net gains on investments: Estimated to come in around $1 billion in 2024.

- The big driver will be the FFH-TRS position. $250 x 1.96mn shares = $500 million?

- Remaining mark to market holdings of $7 billion x 6% return = $500 million?

10.) Gain on sale/deconsol of insurance sub: This is where I put the large asset sales/revaluations.
- In 2023, it was the sale of Ambridge and the revaluation of GIG for a total of $550 million.
- In 2024, I am modelling a gain of $300 million. Perhaps Fairfax (finally) gets approval from regulators in India to move their ownership in Digit from 49% to 68% and this generates a sizable gain. A Digit IPO might also result in a write up of Fairfax's position.

Bottom line, this bucket is a wild card. But Fairfax has a long history of surfacing significant value hidden on its balance sheet. $300 million per year seems like a conservative average estimate. I am including insurance and non-insurance here together (even though the title says insurance).

11.) Income taxes: estimated at 19% (historical average rate)

12.) Non-controlling interests: I am expecting Fairfax to take out one of its minority partners in 2024. The leading candidate is Brit. My second choice would be increasing their ownership in Allied World to 90% (from 83.4%).
- In the past, I used an average rate of 11% (amount of net earnings that was allocated to non-controlling interests). This has been reduced to 9.5% in 2024 and 7.5% in 2025.
- This change increases the amount of net earnings going to Fairfax shareholders.

13.) Shares Outstanding: Estimated that effective shares outstanding will be reduced by 300,000 shares per year for 2024 and 2025. This is the same amount as 2023.

Notes:

- 'Underwriting profit': Includes insurance and reinsurance; does not include runoff or Eurolife life insurance.
- 'Interest and dividends' and 'share of profit of associates': Includes insurance, reinsurance and runoff.

Return on Equity Calculation

Return on equity (ROE) is calculated below using 'average equity' which is:

- (PY ending BV/share + CY ending BV/share) / 2

I think most of the industry (other P/C insurance companies, analysts) calculate ROE using an average number for equity. So, this likely makes my ROE estimates more comparable with industry numbers.

The Building Blocks Used as Inputs to Our Forecasting Model

- Net Premiums and Underwriting Profit
- Interest and Dividend Income
- Share of Profit of Associates
- Investment Gains

Net Premiums, Combined Ratio and Underwriting Profit

March 10, 2024

At its core, Fairfax Financial is an insurance company.

Underwriting profit is one of the core inputs used to estimate earnings for P&C insurance companies. Along with interest and dividend income, it is also considered a high-quality source of earnings by investors.

Net Premiums Earned x (1 - Combined Ratio) = Underwriting Profit

Net Premiums

The size of Fairfax's insurance business has increased dramatically over the past 7 years (2016-2023). Net premiums written have increased from $8.1 billion in 2016 ($350/share) to $22.9 billion in 2023 ($996/share), which is total growth of 183% and a CAGR of 16% per year. That is a big increase.

What has driven this significant growth? Two very different factors have been responsible:

- From 2016-2018, acquisitions were responsible for much of the growth.
    - Brit (2015), International (2016) and Allied World (2017).
- From late 2019 to today most of the growth has been organic, the result of the hard market in insurance.

Looking back, Fairfax timed their large insurance acquisitions perfectly - right before the hard market started in late 2019.

My current forecast is for Fairfax to grow net premiums written by $2.7 billion = 12% in 2024, to $25.6 billion. This growth will be primarily driven by two factors:

- Fairfax's acquisition of Gulf Insurance Group closed in late 2023. This will add about $1.7 billion in net written premiums in 2024.
- The hard market in insurance is continuing in 2024. My guess is this will add $1 billion in net written premiums in 2024, which is growth of 4.4%.

Combined ratio (CR)

Two key inputs in estimating the combined ratio are catastrophe losses and reserve releases.

Catastrophe losses

This is the big wild card every year.

- 2023 was a below average year for catastrophes, coming in at 4.0 CR points. This will likely be a headwind in 2024 as catastrophe losses normalize at a higher level.
- Fairfax has been modestly shrinking its catastrophe exposure, primarily at Brit. This should modestly shrink catastrophe losses moving forward. This should be a small tailwind.

Current Period Catastrophe Losses

	Fourth quarter				Year ended December 31,			
	2023		2022		2023		2022	
	Losses(1)	Combined ratio impact(2)	Losses(1)	Combined ratio impact(2)	Losses(1)	Combined ratio impact(2)	Losses(1)	Combined ratio impact(2)
Hawaii wildfires	3.3	0.1	—	—	183.6	0.8	—	—
Turkey earthquake	1.2	—	—	—	113.0	0.5	—	—
Italy hailstorms	30.8	0.5	—	—	47.2	0.2	—	—
Hurricane Ian	—	—	6.4	0.2	—	—	567.0	2.8
France hailstorms	—	—	22.8	0.4	—	—	118.7	0.6
Australian floods	—	—	(2.4)	—	—	—	71.4	0.3
Other	146.6	2.6	130.4	2.4	553.5	2.5	498.6	2.4
Total catastrophe losses	181.9	3.2	157.2	3.0	897.3	4.0	1,255.7	6.1

(1) Net of reinstatement premiums.

(2) Expressed in combined ratio points.

Reserve releases

- Reserve releases at Fairfax increased in 2023 to a benefit of 309.6 million, which represents 1.4 CR points. If reserve releases continue at this level in 2024 it will be a tailwind.

Net (Favourable) Adverse Prior Year Reserve Development

	Fourth quarter		Year ended December 31,	
	2023	2022	2023	2022
Northbridge	(29.0)	(15.3)	(75.9)	(33.1)
Crum & Forster	(0.1)	(0.1)	(0.5)	(0.5)
Zenith National	(19.7)	(8.9)	(50.8)	(43.6)
North American Insurers	(48.8)	(24.3)	(127.2)	(77.2)
Allied World	1.4	(0.1)	—	30.5
Odyssey Group	(86.1)	(45.7)	(78.6)	(49.9)
Brit	(2.8)	9.6	(3.0)	(1.7)
Global Insurers and Reinsurers	(87.5)	(36.2)	(81.6)	(21.1)
International Insurers and Reinsurers	(15.4)	(18.1)	(100.8)	(97.9)
Property and casualty insurance and reinsurance	(151.7)	(78.6)	(309.6)	(196.2)

Underwriting profit

Fairfax finished 2023 with a combined ratio (CR) of 93.2%, which resulted in a record underwriting profit of $1.5 billion. My current estimate is for Fairfax to finish 2024 with a CR of 95%, which would deliver an underwriting profit of about $1.24 billion in 2024.

Bottom line, the combination of growing net premiums and solid (and improving) underwriting has Fairfax poised to deliver another very good underwriting profit in 2024.

Important: My numbers do NOT include runoff - to keep them consistent with how Fairfax reports and discusses results.

Fairfax: Net Premiums and Underwriting Profit
Updated: March 10, 2024

	Net Premiums Written			Net Pr Earned			UW Profit		YE
		YOY	Per		YOY	CR	Profit	Per	share
	$bn	Change	Share	$bn	Change	%	$mn	Share	count
2016	$8.1	8%	$350	$7.9	7%	92.5	$576	$22	23.1
2017	$10.0	23%	$359	$9.7	24%	106.6	-$642	-$25	27.8
2018	$12.0	20%	$442	$11.9	23%	97.3	$318	$12	27.2
2019	$13.3	10%	$495	$12.5	5%	96.9	$395	$15	26.8
2020	$14.7	11%	$562	$13.9	11%	97.8	$308	$12	26.2
2021	$17.8	21%	$745	$15.5	12%	95.0	$801	$31	23.9
2022	$22.3	25%	$957	$21.0	35%	94.7	$1,105	$47	23.3
2023	$22.9	3%	$996	$22.2	6%	93.2	$1,522	$66	23.0
2024E	$25.6	12%	$1,130	$24.9	12%	95.0	$1,243	$55	22.7
2025E	$26.4	3%	$1,179	$25.6	3%	95.0	$1,280	$57	22.4

Interest and Dividend Income

March 10, 2024

Let's start with the big picture.

<u>How importance is interest and dividend income to Fairfax?</u>

Interest and dividend income is Fairfax's most important income stream for a couple of reasons.

- Size: at more than 40%, it is the largest driver of operating income.
- Quality: it is considered a high-quality source of earnings because it tends to be quite stable year to year.
- Rapid growth in recent years: higher interest rates has spiked interest income.

Fairfax - Drivers of Operating Income		
	2023	split
Underwriting profit - ins & reins.	$1,522	34%
Interest & dividend income	$1,896	43%
Share of profit of associates	$1,022	23%
Operating income	**$4,441**	

<u>What are the components and what are their relative sizes?</u>

Interest and dividend income is made up of three parts:

- <u>Interest income</u>: received from the fixed income portfolio (cash, short term investments, bonds, derivatives and other invested assets)
- <u>Dividends</u>: received from equity portfolio (common and preferred stocks)
- <u>Investment expenses</u>: Fairfax's investment portfolio is managed by Hamblin Watsa.

Interest income is the big item – so it will get most of the attention in this post.

Fairfax - Split of Interest and Dividend Income (mn $)	2023	split
Interest Income	$1,841	93%
Dividends	$134	7%
Expenses	-$79	n/a
Total	**$1,896**	

<u>Estimating expenses and dividend income for 2024</u>

Let's start with expenses, as it is the easiest item to forecast. Expenses totalled $79 million in 2023. We will use $80 million as our estimate for both 2024 and 2025.

Dividend income totalled $139 million in 2024. Eurobank confirmed they will likely start paying a dividend of €0.06/share in 2H 2024. This would increase dividend income by $83 million.

As a result, we should see dividend income increase materially in 2024. We will use $170 million as our estimate for dividends for 2024 and $210 million for 2025. We will adjust these estimates once we get clarity on the Eurobank dividend (amount and timing) likely later in Q2.

Eurobank Dividend - Est FFH Payout			
Dividend Estimate	FFH Shares	Possible Payout € mn	$ mn
€ 0.06	1,266	€ 76	$83
Euro to US$		$1.088	

Estimating interest income for 2024 – a deep dive

Given its importance to Fairfax, for interest income we are going to go into some detail.

Two items drive interest income:

- The size of the fixed income portfolio
- The average yield earned on the investments held in the portfolio

A review of the size of the fixed income portfolio.

The fixed income portfolio at Fairfax increased in size from $20.3 billion in 2016 to $45.0 billion in 2023. The total increase over the past 7 years was 122% and the CAGR was 12%.

Fairfax: Fixed Income Portfolio Review
March 10, 2024

	$bn	Change	Comments: Drivers of change in portfolio
2016	$20.3		
2017	$28.0	37.9%	Allied World acquisition.
2018	$26.7	-4.6%	First Capital sale.
2019	$26.3	-1.5%	Runoff Sale (Riverstone UK)
2020	$29.8	13.3%	Hard market starts.
2021	$36.8	23.5%	Hard market accelerates.
2022	$38.9	5.7%	Hard market continues. Bond bear market (headwind).
2023	$45.0	15.7%	Hard market. Strong earnings. GIG acquisition late Dec.

A review of interest income and the average yield of the fixed income portfolio.

Total interest income at Fairfax increased from $514 million in 2016 to $1.8 billion in 2022. The total increase over the past 7 years was 258% and the CAGR was 20%.

The average yield on the fixed income portfolio from 2016-2022 was 2.4%. Yes, that is a very low number. During this time, Fairfax was positioned very conservatively - high quality and low duration.

The average yield on the fixed income portfolio in 2024 was 4.4%. This is a significant increase from the period from 2016-2022. Interest rates spiked in 2022 and 2023 - having a very low duration fixed income portfolio at the end of 2021 (of 1.2 years) resulted in a very rapid earn-through to interest income.

Fairfax: Interest Income Review
March 10, 2024

	Fixed Income $bn	Total Interest Income $mn	Change %	Avg Yield
2016	$20.3	$514	13%	2.5%
2017	$28.0	$515	0%	2.1%
2018	$26.7	$744	45%	2.7%
2019	$26.3	$826	11%	3.1%
2020	$29.8	$717	-13%	2.6%
2021	$36.8	$568	-21%	1.7%
2022	$38.9	$874	54%	2.3%
2023	$45.0	$1,841	111%	4.4%

Note: we have calculated Average Yield using average Total Fixed Income ((CY+PY)/2).

<u>Summary of current situation</u>

Over the past 7 years, the size of Fairfax's fixed income portfolio has increased 122% to $45 billion. At the same time, the average yield on the portfolio has increased 73% to 4.4%. As a result, interest income has dramatically increased by 258% to $1.8 billion = CAGR of 20%.

Fairfax ended 2023 exceptionally well positioned.

<u>Forecast for interest income for 2024</u>

To increase accuracy, we are going to build our forecast for interest income by quarter. This will allow us to layer in our key assumptions in a more thoughtful manner. Unfortunately, beginning in 2023, when reporting quarterly results, Fairfax only reported a total number for interest and dividend income. We do get the split for the full year of 2023. As a result, we are required to make some assumptions to estimate the quarterly split.

My estimate is interest income in Q4, 2023 was about $525 million. This is the baseline we will use for our 2024 forecast. We now need to overlay the key swings. Below are the ones I see:

Tailwind: Increase in size of total fixed income portfolio

- GIG: $2.4bn x 3.5%? = $80mn = $20mn/Q. Start Jan.
- Top line growth: $1bn x 4% = $40mn / 2 = $20mn = $5mn/Q. Start Jan.
    - Growth in premiums – continuation of P/C insurance hard market
    - Reinvestment of part of retained earnings

Neutral: Interest rate pickup: the majority of this benefit is likely already reflected in our Q4 interest income estimate of $525 million.

Headwind: Rate cuts by global central banks in 2H 2024.

- $9bn x .0075% = $70mn/year = $20mn/Q. Start June.

Bottom line, the tailwinds in 2024 appear greater than the headwinds. As a result, my current estimate is for interest income to come in around $2.14 billion in 2024, which is an increase of 16% from $1.84 billion in 2023. This would put the average yield on the fixed income portfolio at about 4.7% - which is about twice as much as the average from 2016-2022.

Fairfax: Interest Income by Quarter								**Fixed**	**Avg**
March 10, 2024			**Q1**	**Q2**	**Q3**	**Q4**	**FY**	**Income**	**Yield**
2022	Interest		$153	$176	$230	$314	**$873.5**	$38.9	2.2%
	Dividends		$28	$43	$39	$31	**$140.4**		
	Expenses		-$12	-$17	-$12	-$11	**-$52.1**		
	Total I&D		**$169**	**$203**	**$257**	**$333**	**$961.9**		
2023	Interest	est	$371	$449	$496	$525	**$1,841**	$45.0	4.4%
	Dividends	est	$31	$31	$32	$40	**$134**		
	Expenses	est	-$20	-$15	-$15	-$29	**-$79**		
	Total I&D		**$382.3**	**$464.6**	**$512.7**	**$536.4**	**$1,896**		
2024	Interest	est	$540	$540	$535	$525	**$2,140**	$47.0	4.7%
	Dividends	est	$30	$30	$55	$55	**$170**		
	Expenses	est	-$20	-$20	-$20	-$20	**-$80**		
	Total I&D		**$550.0**	**$550.0**	**$570.0**	**$560.0**	**$2,230**		
2025	**Tot I&D**	est	$550	$550	$550	$550	**$2,200**		

Is the increase in interest income sustainable?

Yes. During 2023, Fairfax increased the average duration of the fixed income portfolio from 1.6 years to more than 3 years. Fairfax estimates interest and dividend income is tracking to be +$2 billion each of the next 4 years (with no guarantees, of course).

Summary: Interest and Dividend Income

Coming full circle, let's now sum together each of the estimates for interest income, dividends and expenses. Interest and dividend income is forecasted to come in at about $2.23 billion in 2024, an increase of 18% over 2023. This income stream represents 50% of forecasted operating earnings for Fairfax in 2024.

Fairfax: Fixed Income Portfolio - Interest & Dividend Income										
Updated: March 10, 2023										
		A+B+C			A			B	C	
	Total Fixed Income $bn	Total Interest Dividend $mn	YOY change	per share	Interest $mn	Per Share	Yield	Divid. $mn	Invest. Expen. $mn	YE share count mn
2016	$20.3	$555	8%	$24	$514	$22	2.5%	$67	-$26	23.1
2017	$28.0	$559	1%	$20	$515	$19	2.1%	$73	-$29	27.8
2018	$26.7	$784	40%	$29	$744	$27	2.7%	$82	-$42	27.2
2019	$26.4	$880	12%	$33	$826	$31	3.1%	$94	-$40	26.8
2020	$29.8	$769	-13%	$29	$717	$27	2.5%	$78	-$25	26.2
2021	$36.8	$641	-17%	$27	$568	$24	1.7%	$108	-$36	23.9
2022	$38.9	$962	50%	$41	$874	$37	2.3%	$140	-$52	23.3
2023	$45.0	$1,896	97%	$82	$1,841	$80	4.4%	$134	-$79	23.0
2024E	$47.0	$2,230	18%	$98	$2,140	$94	4.7%	$170	-$80	22.7
2025E	$49.0	$2,200	-1%	$98	$2,075	$93	4.3%	$210	-$85	22.4

Share of Profit of Associates

March 10, 2024

Over the past two years, share of profits of associates has become a very important source of earnings for Fairfax. At over $1 billion it has become a very big income stream. And, together with underwriting profit and interest and dividend income, it forms the third leg of all-important operating earnings for Fairfax.

What is share of profit of associates?

Fairfax has a very large equity portfolio – as of March 8, it has a total valued of about $19 billion (including the FFH-TRS position at its notional value). From an accounting perspective, equity holdings generally fall into one of three buckets – primarily based on how much of the company Fairfax owns and how much control it exerts.

As we can see in the chart below, holdings that fall in the 'Associates' bucket represent about $7 billion or 38% of Fairfax's total equity portfolio. For each of these holdings, Fairfax has an ownership position of more than 20% but less than 50%, and also exerts significant influence but not control.

From an accounting perspective, Associates holdings are equity accounted - what matters is how much these companies actually earn each quarter (pre-tax). This is the number that Fairfax reports each quarter – adjusted for their ownership percent – in the share of profit of associates bucket in the income statement.

Fairfax: Equity Portfolio: Split by Accounting Treatment				
	March 8, 2023		Own / control	
A.) Mark to market	$ 8,980	47%	Own < 20%	
B.) Associates	$ 7,109	38%	Own 20 to 50%	Significant influence but not control
C.) Consolidated	$ 2,838	15%	Own > 50%	Control
Total Equity Portfolio	**$18,926**	**100%**		

Share of profit of associates provide a good source of look-through earnings for Fairfax investors – providing a view of the actual performance of the various associates equity holdings (versus simply following the change in the stock price).

Balance sheet impact: The share of profit of associates amount is also the number that is used to increase (decrease in the case of a loss) the carrying value on the balance sheet of each associate equity holding (less any dividends received).

The big picture

Over the 3-year period, from 2019-2021, share of profit of associates at Fairfax averaged $143 million per year. In 2022, it was $1 billion. That surprised me. That was a big increase over the trend from the previous years. But 2022 must be an outlier and Fairfax should settle back to something closer to $200 million in 2023… right? Wrong. In 2023, share of profits of associates again came in at $1 billion – and this was despite the significant headwind caused by the sale of Resolute Forest Products, which contributed $159 million in 2022.

What happened to cause the significant increase over the trend from 2019-2021?

Put simply, the earnings power of the equity holdings captured in the 'associates-equity accounted' bucket is beginning to shine through:

- Eurobank: This holding has become the star of the group. After long 8 years, the turnaround at Eurobank is complete. Eurobank is also benefitting from higher interest rates and a strong economy in Greece. The acquisition of Hellenic Bank looks solid and should boost EPS in 2024/25. The management team at Eurobank has been executing exceptionally well in recent years.
- Poseidon/Atlas: Poseidon is growing rapidly driven by its aggressive new-build strategy. Despite some near-term challenges (caused by higher interest rates), in the 2023AR Prem stated "Poseidon is expected to make net earnings in excess of $400 million in 2024 and $500 million in 2025." Fairfax has a 43% ownership position in Poseidon.
- EXCO Resources: EXCO, a US natural gas producer, performed very well in 2023 (despite the weakness in gas prices). Results for this holding will be volatile.

- Stelco: a new addition to the Associates bucket in late 2022 (when Fairfax's ownership moved to 23%). Led by Alan Kestenbaum, Stelco is exceptionally well managed. Results at Stelco will be tied to the fortunes of the steel industry.
- Fairfax India: the results of the Associates holdings in Fairfax India's portfolio are included here. These holdings, as a group, performing well in 2023.

Over the past 5 years, Fairfax has quietly built out another significant source of earnings that will benefit shareholders for years to come - its collection of 'Associates – Equity Accounted' holdings.

Important swings:

- 2023 removal of holding: The sale of Resolute Forest Products closed in 2023. As a result, $159 million that RFP delivered in 2022 was removed from the Associates bucket in 2023. This was a significant headwind that Fairfax was able to overcome in 2023.
- 2024 removal of holding: The purchase of the Gulf Insurance Group closed in December of 2023. Results for GIG are now consolidated at Fairfax (included in international insurance). We removed $43 million from the Associates bucket when building out 2024 forecast.

2024 forecast

Share of profit of associates is expected to come in at $1.05 billion in 2024, a small increase from 2023.

Fairfax: Share of Profit of Associates
Updated: March 10, 2024

	2019	2020	2021	2022	2023	Est 2024
Eurobank	$0	-$12	$162	$263	$438	$440
Atlas (was Seaspan	$84	$116	$70	$258	$150	$180
EXCO	$22	-$5	-$41	$82	$129	$75
Stelco	$0	$0	$0	$0	$24	$75
Resolute Forest Pro	-$5	-$57	$76	$159	$0	$0
Fairfax India	$230	-$18	$34	$132	$152	$160
Gulf Insurance	$15	$6	$56	$53	$43	$0
Digit	-$8	$9	$5	-$11	$43	$50
All other	-$169	-$153	$41	$78	$87	$120
Grand Total	**$170**	**-$113**	**$402**	**$1,015**	**$1,022**	**$1,050**

Operating Income of Non-insurance Consolidated Companies

March 22, 2024

Over the past couple of years Fairfax has been materially increasing the size of its non-insurance consolidated holdings. Revenue and 'normalized' earnings have been moving higher. However, the improving results over the past 2 years has been masked by large temporary or one-time write-downs/losses - so most investors are not aware of the many positive changes that have been happening under the hood. My guess is the earnings power for this group of holdings will begin to shine through fully in 2024. In the coming years, this bucket is poised to become a much more important income stream for Fairfax - in terms of size and consistency.

Let's begin by getting some context.

The big picture

Fairfax has a very large equity portfolio – as of March 8, it has a total value of about $19 billion (including the FFH-TRS position at its current notional value of $2 billion). From an accounting perspective, equity holdings can be grouped into one of three buckets – based on how much of the company Fairfax owns and how much control it exerts.

In this post we are going to review the equity holdings that fall into the 'Consolidated' bucket. These are the holdings where Fairfax owns more than 50% (or has more than 50% voting control) and therefore has a control position.

The common stock 'Consolidated' holdings have a total value of about $2.8 billion, which is about 15% of Fairfax's total common stock portfolio. I don't think holdings like AGT Food and Ingredients and Sporting Life are included in the $2.8 billion. Bottom line, the group of 'Consolidated' holdings likely has a market value of well over $3 billion.

Fairfax: Equity Portfolio: Split by Accounting Treatment				
	March 8, 2023		Own / control	
A.) Mark to market	$ 8,980	47%	Own < 20%	
B.) Associates	$ 7,109	38%	Own 20 to 50%	Significant influence but not control
C.) Consolidated	$ 2,838	15%	Own > 50%	Control
Total Equity Portfolio	**$18,926**	**100%**		

From an accounting perspective, the results of 'Consolidated' holdings are captured on the Consolidated Statements of Earnings in the 'Non-insurance revenue' and the 'Non-insurance expenses' line items.

What holdings are captured in this bucket?

Below is a list of all the companies - with a brief description of their primary business - that are included in the 'Consolidated' bucket.

Non-insurance Companies		Primary Business
Restaurants & Retail		
	Recipe	Franchisor, owner and operator of restaurants
	Sporting Life Group	Canadian sports lifestyle retail organization (incl Golf Town)
	Other	
Fairfax India		Invests in public and private Indian businesses
Thomas Cook India		
	Thomas Cook India	Provider of integrated travel and travel-related financial services
	Sterling Holiday Resorts	Owner and operator of holiday resorts
Other		
	Grivalia Hospitality	Hospitality real estate investor, developer and manager
	AGT Food & Ingredients	Originator, processor and distributor of value-added pulses and staple foods
	Dexterra Group	Provider of Infrastructure support services
	Boat Rocker	Entertainment content creator, producer and distributor
	Farmers Edge	Provider of advanced digital tools for agriculture

<u>Non-insurance companies</u>

This reporting segment is comprised as follows:

- Restaurants and retail – Comprised principally of Recipe, Golf Town, Sporting Life and Toys "R" Us Canada (deconsolidated on August 19, 2021).
- Fairfax India – Comprised of Fairfax India and its subsidiaries, which are principally NCML and Privi (deconsolidated on April 29, 2021).
- Thomas Cook India – Comprised of Thomas Cook India and its subsidiary Sterling Resorts.
- Other – Comprised primarily of AGT, Dexterra Group, Boat Rocker, Farmers Edge, Grivalia Hospitality (consolidated July 5, 2022), Pethealth (deconsolidated on October 31, 2022) and Mosaic Capital (deconsolidated on August 5, 2021).

<u>How much of each holding does Fairfax own? And what is the value?</u>

The information below is from page 15 of Fairfax's 2023AR and captures what they call the 'common stock holdings.' My guess is their list does not capture a couple of important holdings: AGT Food and Ingredients, Sporting Life and possibly Meadow Foods. We were given the carrying value for Sporting Life in a different section so I have added that. However, we were not given a carrying value for AGT or Meadow and I have not bothered to guess. So, the total for both carrying value and market value in the chart below are likely understated by quite a bit.

Interestingly, the excess of market value to carrying value for this collection of holdings is about $373 million. This number is also likely understated by quite a bit.

Non-insurance Companies		Fairfax's	Market Value		Carrying Value	
	Shares	Ownership	Per share	Total	Per share	Total
Restaurants & Retail						
Recipe (1)	49.4	84.0%	$13.83	$684	$13.83	$684
Sporting Life Group		88.5%		$62		$62
Other						
Fairfax India	57.6	42.5%	$15.20	$875	$13.17	$758
Thomas Cook India	300.3	64.6%	$1.63	$490	$0.67	$201
Thomas Cook India		64.6%				
Sterling Holiday Resorts		64.6%				
Other						
Grivalia Hospitality (1)	339.4	85.2%	$1.67	$567	$1.67	$567
AGT Food & Ingredients		59.6%				
Dexterra Group	31.8	49.3%	$4.28	$136	$3.41	$109
Boat Rocker	25.3	44.9%	$0.95	$24	$3.31	$84
Farmers Edge		61.2%	$0.30		$0.00	$0
Total				**$2,838**		**$2,465**
Excess of Market Value over Carrying Value				**$373**		

Fairfax has voting control over Fairfax India, Dexterra and Boat Rocker.
(1) Market value shown for unlisted consolidated stocks is Fairfax's carrying value

<u>What do the financials look like for this group of holdings?</u>

Over the past three years, revenue has increased 39% to $6.6 billion. However, pre-tax income has been low and stagnant, averaging about $60 million over the past three years.

Non-insurance Companies				Pre-tax	
	Revenue		Expenses	Income	'One-time' losses
2020	$4,742		$4,868	-$126	
2021	$5,158	9%	$5,092	$65	
2022	$5,582	8%	$5,521	$61	Farmers Edge ($133.4 impairment)
2023	$6,615	19%	$6,569	$46	Farmers Edge ($112), Boat Rocker ($26), Grivalia Hospitality ($66)

Below is the split by reporting segment.

Non-insurance Companies	2023		Pre-tax	2022		Pre-tax	2021		Pre-tax	2020		Pre-tax
	Revenue	Expenses	Income	Revenue	Expenses	Income	Revenue	Expenses	Income	Revenue	Expenses	Income
Restaurants & retail	$1,772	$1,691	$82	$1,710	$1,582	$128	$1,804	$1,725	$79	$1,734	$1,811	-$77
Fairfax India	$263	$251	$12	$217	$208	$9	$228	$207	$21	$313	$306	$7
Thomas Cook India	$942	$907	$35	$611	$601	$10	$249	$293	-$44	$225	$288	-$63
Other	$3,637	$3,720	-$83	$3,044	$3,130	-$86	$2,876	$2,867	$9	$2,470	$2,463	$8
Total	**$6,615**	**$6,569**	**$46**	**$5,582**	**$5,521**	**$61**	**$5,158**	**$5,092**	**$65**	**$4,742**	**$4,868**	**-$126**

Notes:

- Pre-tax income (loss) before interest expense; excludes interest and dividends, share of profit (loss) of associates and net gains (losses) on investments.
- The majority of Fairfax India's earnings fall into the 'Share of Profit of Associates' bucket.

<u>What is driving the significant top line growth?</u>

- Improving fundamentals: Companies in this bucket of holdings were significantly impacted by Covid, which was a significant drag on results from 2020 to 2022. Recipe (full serve, dine-in restaurants), Thomas Cook India (travel) and Dexterra (facilities management). Results from these these companies rebounded in 2023.
- Significant new addition: Grivalia Hospitality was added in 2022 when Fairfax increased its stake from 33.5% to 78.4% at a cost of $195 million. The position was increased further in 2023 to 85.2%.
- Significant increases in ownership: in 2022, Fairfax increased its stake in Recipe from 46% to 84% at a cost of $342 million. In 2022, Fairfax increased its stake in Sporting Life from 71% to 88.5% (funded via retained earnings).
- There also were a few notable sales / deconsolidations:
    - Restaurants & retail: Toys "R" Us Canada (deconsolidated on August 19, 2021)
    - Fairfax India: Privi (deconsolidated on April 29, 2021).
    - Other: Pethealth (deconsolidated on October 31, 2022) and Mosaic Capital (deconsolidated on August 5, 2021).

Bottom line, top line should grow nicely in 2024 and future years. And now a much larger share of earnings for these companies will flow through to Fairfax shareholders.

<u>Pre-tax income at this group of holdings has been low the past four years due to significant temporary or one-time items.</u>

As mentioned already, Covid was a significant headwind for Recipe, Thomas Cook India and Dexterra from 2020 to 2022. Thomas Cook India had a fantastic 2023. Recipe continues to right-size its business/structure/systems after a decade of rapid consolidation.

Farmers Edge took very large write downs in 2022 ($133.4 million) and 2023 ($112 million in losses) and the business is now carried at a $0 valuation. It was taken private by Fairfax in March of 2024. My guess is this business will stop bleeding money later in 2024.

Boat Rocker also saw a write down in 2023 ($26 million). This is now a small holding for Fairfax.

Grivalia Hospitality took a loss of $66 million in 2023. For the past couple of years, Grivalia has been investing heavily in building out its collection of ultra-high luxury resorts. 5 are now open. Revenue should materially increase in 2024. The company is pivoting its business from the investment phase to the operating phase which should lead to improving financial results.

The significant temporary / one-time events of the past couple of years will likely decline in size moving forward. Headwinds will become tailwinds. And when they do, the earnings power of this collection of businesses will be released like a coiled spring.

Summary

The companies in this bucket of holdings have been undergoing significant positive changes over the past couple of years. (Just like the rest of Fairfax's equity holdings.)

Poor performers are being wound down. Underperforming companies have been executing turn-around plans for the past couple of years and improved results are starting to show up. New holdings have been added in recent years. And Fairfax owns more of existing holdings.

Bottom line, the intrinsic value of the companies captured in this bucket has been increasing over the past three years. We should see earnings start to improve in the coming years. This group of companies is poised to become another meaningful and growing income stream for Fairfax.

Earnings estimate for 2024 and 2025

My current estimate is for this collection of holdings to deliver pre-tax earnings of $150 million in 2024 and $200 million in 2025. These estimates could prove to be very conservative.

A strategy question:

Do we see Fairfax continue to build out this bucket of companies? Do they aspire to become more of a holding company like Berkshire Hathaway in the coming years?

Are there strategic advantages to Fairfax of having a few large wholly owned cash generating equity holdings to complement their P/C insurance business?

I don't think Fairfax wants to go full Berkshire in the coming years. Unlike Berkshire, at the appropriate time, Fairfax sells assets - I expect Fairfax will monetize one or more of its non-insurance consolidated holdings in the coming years. And I suspect it is still a priority for Fairfax to grow its P/C insurance business.

> "As the table on page 15 shows, the consolidated investments include the following: Recipe, Fairfax India, Grivalia Hospitality, Thomas Cook India, Dexterra Group and Boat Rocker Media. Our consolidated investments are significant, producing total revenue of $6.6 billion and pre-tax income of $271 million in 2023. Fairfax India had pre-tax income of $380 million, Recipe $38 million, Thomas Cook $27 million and Dexterra $29 million. Those were offset by losses at Grivalia of $66 million, Boat Rocker $26 million and Farmers Edge of $112 million which included impairments of $64 million." *Prem's Letter, FFH 2023AR*

> "As the table on page 13 shows, consolidated investments include the following: Recipe, Fairfax India, Grivalia Hospitality, Thomas Cook India, Boat Rocker Media, Dexterra Group and Farmers Edge. Our consolidated investments are significant, producing total revenue of $5.6 billion, EBITDA of $743 million and pre-tax income of $303 million (excluding a $133 million writedown of Farmers Edge) before minority interest in 2022." *Prem's Letter, FFH 2022AR*

Non-insurance companies

	2023					2022				
	Restaurants and retail(1)	**Fairfax India(2)**	**Thomas Cook India(3)**	**Other(4)**	**Total**	**Restaurants and retail(1)**	**Fairfax India(2)**	**Thomas Cook India(3)**	**Other(4)**	**Total**
Revenue	1,772.3	263.3	941.6	3,637.3	6,614.5	1,710.3	216.7	611.0	3,043.6	5,581.6
Expenses	(1,690.7)	(251.4)	(906.5)	(3,720.1)	(6,568.7)	(1,582.2)	(208.1)	(600.8)	(3,129.8)	(5,520.9)
Pre-tax income (loss) before interest expense and other	81.6	11.9	35.1	(82.8)	45.8	128.1	8.6	10.2	(86.2)	60.7
Interest and dividends	9.9	(87.4)	–	1.4	(76.1)	9.9	21.4	–	(4.7)	26.6
Share of profit (loss) of associates	–	151.1	(0.1)	1.2	152.2	(0.1)	132.0	0.3	1.8	134.0
Operating income (loss)	**91.5**	**75.6**	**35.0**	**(80.2)**	**121.9**	**137.9**	**162.0**	**10.5**	**(89.1)**	**221.3**

(1) Comprised primarily of Recipe and Sporting Life Group.

(2) Comprised of Fairfax India and its subsidiaries. These results differ from those published by Fairfax India primarily due to Fairfax India's application of investment entity accounting under IFRS Accounting Standards.

(3) Comprised of Thomas Cook India and its subsidiaries including Sterling Resorts. These results differ from those published by Thomas Cook India primarily due to differences between IFRS Accounting Standards and Ind AS, and acquisition accounting adjustments.

(4) Comprised primarily of AGT, Dexterra Group, Boat Rocker, Farmers Edge and Grivalia Hospitality (consolidated on July 5, 2022).

For details of acquisition and divestiture transactions, refer to the Business Developments section of this MD&A under the heading "Acquisitions and Divestitures".

Restaurants and retail

The increase in revenue and expenses of Restaurants and retail in 2023 primarily reflected higher business volumes at Recipe principally due to the absence of COVID-19 related restrictions in 2023 compared to 2022. The increase in revenue in 2023 also reflected higher menu prices due to inflationary pressures. The increase in expenses in 2023 also reflected higher costs of sales relating to food inflation and compensation expense at Recipe and higher expenses related to new store openings at Sporting Life Group.

Fairfax India

The increase in revenue and expenses of Fairfax India in 2023 primarily reflected the consolidation of Maxop by Fairfax India during 2022, partially offset by decreased revenue and expenses at Fairchem Organics principally due to decreases in sales prices and costs of sales.

Interest and dividends included the impact of Fairfax India's performance fees payable to Fairfax of $69.4 in 2023 compared to a reversal of performance fee payable of $36.4 in 2022. At December 31, 2023 the holding company had a performance fee receivable of $110.2 pursuant to its investment advisory agreement with Fairfax India for the period from January 1, 2021 to December 31, 2023. The company elected to receive the performance fee payable in cash and expects receipt of payment within the first six months of 2024. For additional details refer to note 26 (Related Party Transactions) to the consolidated financial statements for the year ended December 31, 2023.

Thomas Cook India

The increase in revenue and expenses of Thomas Cook India in 2023 primarily reflected higher business volumes in all segments resulting from increased domestic and international travel as the hospitality industry continued to show significant recovery in 2023.

Other

The increase in revenue and expenses of Other in 2023 primarily reflected higher business volumes at AGT, Boat Rocker and Dexterra Group and the consolidation of Grivalia Hospitality (on July 5, 2022), partially offset by the deconsolidation of Pethealth (deconsolidated on October 31, 2022) and a lower non-cash goodwill impairment charge related to the company's investment in Farmers Edge of $63.5 in 2023 compared to $133.4 in 2022.

Investment Portfolio: What Could It Earn in 2024 & 2025?

March 10, 2024

As we complete our earnings estimate for Fairfax, we are able to strip out some of the line items and re-package them in a different way to improve our understanding of the company.

Let's start with the big picture

Fairfax has two economic engines that drive earnings and growth in book value: underwriting and investments. Given their non-traditional P/C insurance business model (significant investments in equities) only about 20% of Fairfax's various income streams come from underwriting and about 80% come from investments.

What rate of return is Fairfax earning on its $65 billion investment portfolio?

That is the question we will answer in this post.

How big is Fairfax's investment portfolio?

It's about $65 billion or $2,826/share (before minority interests).

What is the split?

- Fixed income = $45 billion (69%)
- Equities/Preferred Stock/Other = $22 billion (31%)

Fairfax: Estimated Value of Investment Portfolio

March 10, 2024	$bn	Split
Fixed Income	$45	69.2%
Preferred Stocks / Property	$3	4.6%
Equities / Derivatives	$17	26.2%
Total Investments	**$65**	
Per Fairfax Share	$2,826	

Has the total investment portfolio been growing in size?

Yes. From 2018 to 2023, the total investment portfolio increased from $38.8 billion to $64.8 billion, an increase of 67% = CAGR of 11.8%.

What components will we use to determine Fairfax's total return on its investment portfolio?

1. Interest and dividend income
2. Share of profit of associates
3. Other (revenue – expenses) for non-insurance subsidiaries: Recipe, Grivalia Hospitality, Thomas Cook India, AGT Food Ingredients, Dexterra, Sporting Life and Boat Rocker.
4. Net gains (losses) on investments: in the past this has included gains (losses) from both equities and fixed income. We will assume no gains (losses) from fixed income (moving forward changes in fixed income will likely involve a roughly equal move in the opposite direction from 'effects of discounting and risk adjustment – IFRS 17'). Therefore, our estimate for gain (losses) for 2024 and 2025 will only include changes from equity holdings.
5. Gain on sale/deconsolidation of insurance subs: this is where we put the large one-time gains from sales or revaluations like pet insurance (2022), Ambridge and GIG (2023).
6. Investments in associates: the year-over-year change in excess of fair value over carrying value. This amount is not reflected in Fairfax's financial statements. But it is real value that is being created each year from associate holdings in the equity portfolio that needs to be included in total investment gains.

What did Fairfax earn on its total investment portfolio in the past?

For the 5-year period from 2018 to 2022, Fairfax earned an average total return of 5.1% on its total investment portfolio. Let's overlay what happened in financial markets over this same time period:

- Historically low interest rates from 2018 to the middle 2022 - killed returns of the fixed income portfolio for much of the 5-year period.
- Three different bear markets in stocks: 2018, 2020 and 2022.
- Historic bear market in bonds in 2022.

Given the significant headwinds in financial markets from 2018-2022, the fact that Fairfax was able to deliver a total return of 5.1% each year (on average) is actually pretty impressive. What happened? Fairfax's investment team at Hamblin Watsa started to get their investing mojo back.

	Fairfax - Returns and the Total Investment Portfolio						
	Updated: March 10, 2024	**2018**	**2019**	**2020**	**2021**	**2022**	**2023**
1.)	Interest & dividends	$784	$880	$769	$641	$962	$1,896
2.)	Share of profit of associates	$221	$170	-$113	$402	$1,015	$1,022
3.)	Other (rev-exp) Non-insurance Subs	$264	$104	-$139	$71	$61	$46
4.)	Net gains (losses) on investments	$253	$1,716	$313	$3,445	-$1,734	$1,950
5.)	Gain on sale/deconsol of ins sub	$0	$0	$117	$264	$1,220	$549
6.)	Associates: YOY change in FV vs CV	-$559	$437	-$456	$860	-$148	$317
	Total Investment Return (millions)	**$963**	**$3,307**	**$492**	**$5,683**	**$1,375**	**$5,780**
	Total Investments (billions)	**$38.8**	**$39.0**	**$43.2**	**$53.0**	**$55.5**	**$64.8**
	Average Tot Investments (billions)		**$38.9**	**$41.1**	**$48.1**	**$54.3**	**$60.1**
	Average Return (Annual)	**2.5%**	**8.5%**	**1.2%**	**11.8%**	**2.5%**	**9.6%**
	5 Year Average (2018-2022)	**5.3%**					

What did the management team at Fairfax do from 2018-2022?

Internal:

- Ended equity hedge/shorting strategy. The final short positions (closed out in late 2020) resulted in total losses of $624 million from 2018-2020, or an average of $208 million over each of the three years.
- The underperforming equity holdings (many purchased from 2014-2017) have mostly been fixed. Beginning in 2022, and lead by Eurobank, these holdings have gone from being a headwind to earnings (losing hundreds of millions every year in total) to now being a tailwind (making hundreds of millions every year in total). That is likely an improvement (swing) of +$500 million per year (my numbers are very rough and intended to be directionally accurate). These businesses are also rapidly increasing in value. For associate holdings this increase in value is showing up in growing excess of fair value over carrying value (this is not captured on the balance sheet).
- Since 2018, new equity investments have been very good. They are, in aggregate, performing very well. These holdings are a growing tailwind to earnings. Chug, chug, chug.

External:

- Interest rates bottomed in late 2021: Fairfax sold $5.2 billion in corporate bonds (yielding 1%) and bought short term treasuries and reduced average duration to 1.2 years.
- Interest rates spiked in 2022.
- Covid bear market 2020: got exposure to 1.96 million Fairfax shares at $373/share. Bought back 2 million Fairfax shares in late 2021 at $500/share.
- Bear market 2022: spent billions buying more of companies it already owned often at bear market (attractive) prices.

The investment team at Fairfax has been putting on a clinic on the benefits of active management. **The extreme volatility we have seen in recent years has actually been a big tailwind to Fairfax and its investment portfolio.**

What did Fairfax earn on its total investment portfolio in 2023?

In 2023, Fairfax earned a total return of 9.6%. Importantly, the most of the return was driven by two operating income items - interest and dividends and share of profit of associates. Both fixed income and equity portfolios delivered very good results - and the table is set for this to last for years into the future.

Why? The significant 'internal' drags that were holding down Fairfax's returns from 2018-2022 are gone. And significant new tailwinds have emerged.

Equities:

- No more losses from the equity hedge/short trade.
- The equity purchases from 2014-2017 are now delivering good returns.
- The equity purchases from 2018-to-date continue to perform well.
- Importantly, Fairfax recently boosted their stakes in many companies they already own at bear market (attractive) prices. This will be a tailwind for future earnings.
- Covid headwinds have flipped to tailwinds at BIAL, Thomas Cook India and Recipe.

Bottom line, the underlying earnings power of Fairfax's $17 billion equity portfolio is finally fully delivering on its potential.

Fixed income:

As good as the story is in equities, it is even better in fixed income. Going short duration of 1.2 years in late 2021 was, with hindsight, pure genius. This might be one of the best investment decision Fairfax has made in its history. Bond yields have since spiked higher. As a result, interest income has spiked higher. And in 2023, Fairfax extended the average duration of its fixed income portfolio to over three years – which locks in high interest income for the next 4 years.

The big increases in the returns of both the equity and fixed income portfolios is now spiking the return on Fairfax's $65 billion total investment portfolio. Most importantly, the increase in earnings we are seeing in the equity portfolio (to higher quality) and the bond portfolio (to longer duration) make the much higher earnings durable.

Ok. Enough talk. Show me the money!

What could Fairfax earn on its total investment portfolio in 2024?

My current estimate is for Fairfax to earn a total investment return of $4.9 billion in 2024, or 7.5% on average total investments of $65.9 billion. Note: this number excludes gains (losses) from the fixed income portfolio. For details of what assumptions went into the build for each of the line items below, see the other posts in this chapter.

Importantly, the fixed income and equity portfolios have never been positioned better at Fairfax than they are today. This sets the table nicely for future returns.

	Fairfax - Returns and the Total Investment Portfolio							**2024**	**2025**
	Updated: March 10, 2024	**2018**	**2019**	**2020**	**2021**	**2022**	**2023**	**FY est**	**FY est**
1.)	Interest & dividends	$784	$880	$769	$641	$962	$1,896	$2,230	$2,200
2.)	Share of profit of associates	$221	$170	-$113	$402	$1,015	$1,022	$1,030	$1,100
3.)	Other (rev-exp) Non-insurance Subs	$264	$104	-$139	$71	$61	$46	$150	$200
4.)	Net gains (losses) on investments	$253	$1,716	$313	$3,445	-$1,734	$1,950	$1,000	$925
5.)	Gain on sale/deconsol of ins sub	$0	$0	$117	$264	$1,220	$549	$300	$300
6.)	Associates: YOY change in FV vs CV	-$559	$437	-$456	$860	-$148	$317	$200	$200
	Total Investment Return (millions)	**$963**	**$3,307**	**$492**	**$5,683**	**$1,375**	**$5,780**	**$4,910**	**$4,925**
	Total Investments (billions)	**$38.8**	**$39.0**	**$43.2**	**$53.0**	**$55.5**	**$64.8**	**$67.0**	**$69.0**
	Average Tot Investments (billions)		**$38.9**	**$41.1**	**$48.1**	**$54.3**	**$60.1**	**$65.9**	**$68.0**
	Average Return (Annual)	**2.5%**	**8.5%**	**1.2%**	**11.8%**	**2.5%**	**9.6%**	**7.5%**	**7.2%**
	5 Year Average (2018-2022)	**5.3%**							

Chapter 3: Valuation

In this chapter we are going to look at Fairfax from the perspective of valuation.

Is the stock cheap? If so, how cheap?

There is no 'right' way to value a company. Insurance investors like to use book value as their North Star. Peter Lynch might argue Fairfax is better valued today as a turnaround play. Ben Graham would tell us to use intrinsic value. Perhaps a comparison to peers like Markel and WR Berkley is the best way to value Fairfax. In a high interest rate world, Warren Buffett might suggest we use an analysis that is built around float.

Valuing a company is difficult. Especially a non-traditional insurance company like Fairfax. That has been under-earning for years (meaning historical results are likely understated).

We are going look at Fairfax in a number of different ways. Each way will provide different insights into the company. Hopefully, when we consider at them all together, we will be better equipped to answer the valuation question.

How to value Fairfax – CR, return on investments, ROE & P/BV

March 31, 2024

There is usually no one 'right way' to value a company. Using multiple methods can provide for a more robust analysis. Weighting the different methods can also be helpful. For the past 3 years i have been valuing Fairfax primarily through the lens of a turnaround.

<u>What about today?</u>

Much has changed at Fairfax over the past 3 years.

- Most importantly, the company stopped doing the things that were causing its underperformance.
- It has also fixed most of the problems that were residing in its equity portfolio.
- The management team/Hamblin Watsa has been putting on a clinic in capital allocation.
- The insurance business has been quietly chugging along.

Weave it all together and Fairfax's two businesses - insurance and investment management - are now performing at a high level and delivering record earnings. And they both look very well positioned for the future.

Bottom line, the turnaround at Fairfax is over. Mission accomplished. Truth be told, the turnaround at Fairfax was probably completed a year ago.

<u>So, what is the best way to value Fairfax today?</u>

I think we can start to value Fairfax not primarily as a turnaround but more like a normal P/C insurance company.

Historical results are starting to become useful for investors as an indicator of future performance. The picture of the earnings power of 'new Fairfax' is slowly coming into focus for investors.

<u>What are the key metrics we should be looking at to value a P/C insurance company?</u>

The two most important metrics are:

- Return on equity (ROE)
- Price to book value (P/BV)

ROE tells us how the company is performing. P/BV tells us how Mr. Market is valuing that performance. Looked at together, these two metrics can provide us with a great deal of insight into how Mr. Market is currently thinking about a company and how it is being valued.

We can unpack ROE. ROE can be looked at as the product of two components:

- Combined ratio (CR)
- Total return on the investment portfolio (TRIP)

In this post we will explore Fairfax's CR, TRIP, ROE and P/BV to see what they tell us about how the company's stock is currently being valued by Mr. Market.

In 2019, Woodlock House Family Capital wrote an article on Fairfax that i have always liked. At the time, it provided a fair assessment of the company. It also provided a short and concise way to value the company using estimates of the combined ratio, total return on investments, ROE and P/BV.

And I love 'the horse story' as a useful mental model when it comes to both life and investing.

- https://www.woodlockhousefamilycapital.com/post/the-horse-story

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So, let's apply the simple framework outlined by Woodlock and see what we can learn about Fairfax's valuation today.

First, let's start by looking at the past.

<u>How did Fairfax do from 2018 to 2022 (average over the 5 year period)</u>

1. CR = 96.3%
2. TRIP = 5.3%

That combination of results delivered an average ROE of 10.1%.

The ROE was very volatile. This was because investment gains (losses) was the biggest component of Fairfax's various income streams from 2018 to 2022 (on average). We had bear markets in stocks in 2018, 2020 and 2022 and an epic bear market in bonds in 2022.

Of interest, despite the crazy volatility in financial markets Fairfax still delivered an average ROE of 10.1% - this performance is likely much better than most investors would have guessed.

Fairfax					
March 31, 2024	**2018**	**2019**	**2020**	**2021**	**2022**
Combined ratio	97.3%	96.9%	97.8%	95.0%	94.7%
Total return on investments	2.5%	8.5%	1.2%	11.8%	2.5%
ROE (average equity)	2.7%	15.9%	1.4%	23.3%	7.2%

5-Year Average From 2018-2022	
Combined ratio	96.3%
Total return on investments	5.3%
ROE (average equity)	10.1%

<u>How did Fairfax do in 2023?</u>

1. CR = 93.2%
2. TRIP = 9.6%

That combination of results delivered an ROE of 22%

Fairfax's performance in 2023 (CR, TRIP and ROE) was a significant improvement from the company's 5-years average (2018-2022).

<u>Was this outperformance a simply the result of a bunch of one-time events? Or is something else going on? Are these much better results sustainable?</u>

To answer these questions, let's review what happened in 2023 at a very top-line level.

<u>Insurance operations</u>:

- The hard market in insurance that started in late 2019 continued to be a tailwind.
- The quality of Fairfax's collection of insurance companies continued to improve.

<u>Investment management</u>:

- The yield of the fixed income portfolio increased from an average of 2.5% from 2018-2022 to 4.4% in 2023. This is a massive increase in yield. In 2023, Fairfax increased the average duration of its $45 billion fixed income portfolio from 1.6 to more than 3 years. This locks in the much higher yield for the next 3 or 4 years. Interest income has exploded higher and the higher amount is sustainable.

- At $2.4 billion, Fairfax's largest equity holding is Eurobank. The Greek economy is now one of Europe's top performing economies. Eurobank has increased substantially in value over the past 36 months and the company looks very well positioned. It is trading today at 6 x EPS - despite the big move higher the stock is still cheap.
- At $2.1 billion, Fairfax's lsecond largest 'equity' holding is FFH - Total Return Swaps (giving Fairfax exposure to 1.96 million Fairfax shares). This position has been an exceptional performer for Fairfax over the past 36 months - and it looks very well positioned looking forward. Despite the big move higher the stock is still cheap (more on this below).
- The overall quality of Fairfax's remaining collection of equity holdings ($14.5 billion) has improved considerably over the past 6 years.

Bottom line, Fairfax's insurance businesses and investment portfolio has never been better positioned in its history than it is today. This suggests the exceptional results Fairfax delivered in 2023 (driven by the CR and TRIP) are not one-time in nature. Rather, it appears Fairfax is entering a period where it could earn a ROE over the next couple of years that is structurally higher than the one it delivered in the recent past (2018-2022).

<u>What is my forecast for Fairfax for 2024?</u>

1. CR = 95%
2. TRIP = 7.4% (details are provided at the end of the post).

This combination of results would deliver an ROE of about 15.8%.

Over the next couple of years, Fairfax is positioned to deliver an average CR of about 95% and a TRIP of around 7.4%. That combination of reported results should result in an ROE that averages a little better than 17% (2023 to 2025).

Importantly, the volatility of this ROE should be less than what was seen from 2018-2022. This is because interest and dividend income has become the largest income stream for Fairfax. Share of profit of associates has also become a very important income stream. Importantly (from a volatility perspective), gains (losses) from investments is no longer the most important driver of earnings for Fairfax.

Fairfax								
March 31, 2024	**2018**	**2019**	**2020**	**2021**	**2022**	**2023**	**2024**	**2025**
Combined ratio	97.3%	96.9%	97.8%	95.0%	94.7%	93.2%	95.0%	95.0%
Total return on investments	2.5%	8.5%	1.2%	11.8%	2.5%	9.6%	7.4%	7.4%
ROE (average equity)	2.7%	15.9%	1.4%	23.3%	7.2%	22.0%	15.8%	14.2%

5-Year Average From 2018-2022	
Combined ratio	96.3%
Total return on investments	5.3%
ROE (average equity)	10.1%

What multiple should a consistent 15% ROE be valued at?

Something starting at around 1.3 x book value seems like a low but reasonable target multiple to use for Fairfax looking out 12 to 24 months.

How is Fairfax valued today?

Fairfax is trading today at a P/BV of 1.15 x (book value at Dec 31, 2023).

For Q1 analysts estimate Fairfax will earn C$59.56/share = US$44.00/share (from Yahoo finance). If we subtract the $15 dividend that was paid by Fairfax in January, we can estimate Fairfax's BVPS at March 31, 2024 = $969/share. This puts Fairfax's 'real time' P/BV at about 1.10 x.

Is a P/BV multiple of 1.10 x reflective of a company that is delivering an ROE of 15% per year? No, a 1.1 x multiple is usually assigned to P/C insurance companies that are poorly managed and expected to deliver poor results in the future (an ROE of less than 10%).

Fairfax (US$)	Mar 31, 2024	
Share Price	$1,079	
2023 Earnings	$187	
P/E	5.8	
	Dec 31, 2023	Dec 31, 2022
Book Value	$940	$762
P/BV	1.15	
ROE (average equity)	22%	

What is the disconnect?

Yes, Fairfax delivered an exceptional ROE of 22% in 2023. Mr. Market is beginning to grasp the fact that Fairfax's earnings have materially increased. But it looks to me like Mr. Market does not yet believe the higher earnings (and ROE) are sustainable. Mr. Market likely expects Fairfax's ROE to quickly return to its historical level of 10%. And for the ROE to be very volatile.

It also should be pointed Fairfax's stock has increase 216% over the past 3.25 years. Clearly Mr. Market has been warming to the Fairfax story over the past couple of years.

Fairfax (US$)	Share Price	YOY change		S&P500	YOY change	
Dec 31, 2020	$341		increase over past 39 months	3,756		increase over past 39 months
Dec 31, 2021	$492	44%		4,766	27%	
Dec 31, 2022	$594	21%		3,840	-19%	
Dec 31, 2023	$921	55%		4,770	24%	
Mar 31, 2024	$1,079	17%	216%	5,254	10%	40%

Let's look into the future.

My current estimate is for Fairfax to earn $160/share in 2024 and $165/share in 2025. I view these estimates as being a reasonable base case (being not overly aggressive or overly conservative).

Using my earnings estimate, it is straight forward to calculate an estimated 2024 year-end book value for Fairfax (we will subtract Fairfax's $15 dividend that is paid in January of each year). We can then add a P/BV multiple to the year-end BV to come up with an estimate of where the shares could trade looking out 12 months. We can compare this estimate to Fairfax's current share price to calculate the potential return for the stock.

Below, we will look at four different P/BV multiples: 1.1, 1.2, 1.3 and 1.4
We will also use two different time frames: 12 months and 24 months.

As stated earlier, I think Fairfax is poised to deliver an average ROE of about 15% over the next couple of years (high and consistent). Therefore, I think a P/BV multiple of 1.3 is a reasonable and conservative multiple to use to value Fairfax - looking out 12 and 24 months. But a range of multiples have been provided so readers can see multiple scenarios.

Estimating the 1-year (12 month) potential return for Fairfax's stock
If Fairfax earned $160/share in 2024 and the stock traded at a P/BV of 1.3x in March of 2025, the stock would deliver a return of about 31% over the next 12 months.

Fairfax	Annual		Year End		Price to Book Value Multiple			
	EPS	Divid.	BV		1.1	1.2	1.3	1.4
Dec 31, 2023			$940					
Dec 31, 2024	$160	$15	$1,085		$1,194	$1,302	$1,411	$1,519
					Stock - 12 Month Return Potential			
Share price March 28, 2024			$1,079		11%	21%	31%	41%

Estimating the 2-year (24 month) potential return for Fairfax's stock

If Fairfax earned $160/share in 2024 and $165/share in 2025 and the stock traded at a P/BV of 1.3x in March of 2026, the stock would deliver a return of about 49% over the next 24 months. Adding in the dividend of $15/share and the total return for shareholders would be about 50%.

Fairfax	Annual		Year End		Price to Book Value Multiple			
	EPS	Divid.	BV		1.1	1.2	1.3	1.4
Dec 31, 2025	$165	$15	$1,235		$1,359	$1,482	$1,606	$1,729
					Stock - 24 Month Return Potential			
Share price March 28, 2024			$1,079		26%	37%	49%	60%

Valuing Fairfax through the lens of a P/C insurer

In 2023, Fairfax delivered a CR of 93.2% and a total return on investments of 9.6%. In turn this delivered an ROE of 22%. In the coming years the company looks poised to deliver an average CR of 95% and a total return on investments of 7.4%. This should enable the company to deliver an ROE of around 17% (2023-2025) with less volatility than past years.

Today, Fairfax is trading at a P/BV multiple of about 1.10x (to estimated BV of $969/share at March 31, 2024). Given its past results and future prospects, this multiple looks very low. Bottom line, despite its monster run the past 3.25 years, the valuation of Fairfax's stock continues to look very cheap.

As Fairfax delivers on its potential, my guess is Mr. Market will continue to warm to the Fairfax story and slowly push the P/BV multiple the company trades at higher.

As a result, future returns for investors in Fairfax will be driven by two factors:

- Earnings
- Increase in multiple

And as we learned earlier, that is a great set-up for patient investors.

Fairfax: My three questions for 2024:

To value a P/C insurance company, in addition to important objective criteria like ROE and P/BV, there are also important subjective criteria to consider:

1. What is the quality of the insurance business?
2. What is the quality of the equity holdings?
3. How good is Fairfax at capital allocation?

The answers to the three questions above will provide important inputs that feed into future earnings and ROE estimates.

I have three separate theses:

1. Fairfax's insurance business is higher quality than investors generally think today. If correct, this suggests Fairfax's future CR could come in better than is currently expected.
2. Fairfax's equity holdings (as a group) have improved markedly in quality over the past 6 years. I don't think this fully recognized by investors today. This suggests to me that future results from the equity portfolio could come in higher than is currently expected. This suggests Fairfax's TRIP could come in better than is currently expected.
3. Fairfax is better at capital allocation than investors generally think today.

If one or more of my theses outlined above proves true that would be a tailwind for future earnings at Fairfax. As Fairfax releases results each quarter in 2024, we will be given important clues.

Bottom line, I think Fairfax is a higher quality company that is generally understood today.

The good news is my 'quality' thesis for Fairfax is not priced into the shares today. Remember, Fairfax currently trades at a P/BV multiple of about 1.1 x. So if my thesis above is wrong there is likely limited downside. However, if my thesis is correct then there is significant upside as the shares get re-rated to a higher multiple. The risk/reward set-up today looks heavily skewed to the upside.

Estimating the total return on the investment portfolio

Below is a chart that estimates the total return on Fairfax's investment portfolio going back to 2018. It also has an estimate for 2024 and 2025.

The key take-aways?

Bigger + higher return:

- The investment portfolio increased in size from $39 billion in 2018 to $65 billion in 2023, which is an increase of 66%.
- Fairfax averaged a total return of 5.3% from 2018-2022. In 2023 the return was 9.6% and the estimate for both 2024 and 2025 is 7.4%. Fairfax is poised to earn a rate of return on its investment portfolio that is 40% higher than what it earned from 2018-2022.

More consistent (less volatile): interest and dividends is now driving more than 40% of the total return. Share of profit of associates is now driving more than 20%. This will greatly reduce the volatility of investment returns in the coming years. In turn, this will greatly reduce the volatility of the ROE (compared to the past).

2024 Investment Portfolio Estimates - Key Assumptions:

1. Interest and dividends: average fixed income portfolio = $46m x 4.7% yield
2. Share of profit of associates: Eurobank = $440m; Poseidon = $180m; Fairfax India = $160m
3. Other - non-insurance consolidated companies: includes Recipe, Thomas Cook India, Grivalia Hospitality, AGT, Dexterra, Sporting Life.
4. Net gains (losses) on investments: FFH-TRS = $500m (1.96m x $250); mark-to-market equities = $500 million ($7b x 7%). Assume no change in fixed income portfolio.
5. One time gain (sale/revaluation): $300m. This will be lumpy from year to year.
6. Associates/consolidated holdings - YOY change in FV vs CV: Eurobank, Thomas Cook India, Stelco etc.

The list above is not all-inclusive. Therefore, it likely understates the actual increase in intrinsic value that will be building at Fairfax's various holdings over time (insurance and non-insurance).

	Fairfax - Returns and the Total Investment Portfolio							2024	2025
	Updated: March 10, 2024	2018	2019	2020	2021	2022	2023	FY est	FY est
1.)	Interest & dividends	$784	$880	$769	$641	$962	$1,896	$2,181	$2,180
2.)	Share of profit of associates	$221	$170	-$113	$402	$1,015	$1,022	$1,050	$1,150
3.)	Other (rev-exp) Non-insurance Subs	$264	$104	-$139	$71	$61	$46	$150	$225
4.)	Net gains (losses) on investments	$253	$1,716	$313	$3,445	-$1,734	$1,950	$1,000	$1,000
5.)	Gain on sale/deconsol of ins sub	$0	$0	$117	$264	$1,220	$549	$300	$300
6.)	Associates: YOY change in FV vs CV	-$559	$437	-$456	$860	-$148	$317	$200	$200
	Total Investment Return (millions)	**$963**	**$3,307**	**$492**	**$5,683**	**$1,375**	**$5,780**	**$4,881**	**$5,055**
	Total Investments (billions)	**$38.8**	**$39.0**	**$43.2**	**$53.0**	**$55.5**	**$64.8**	**$67.0**	**$69.0**
	Average Tot Investments (billions)		**$38.9**	**$41.1**	**$48.1**	**$54.3**	**$60.1**	**$65.9**	**$68.0**
	Average Return (Annual)	**2.5%**	**8.5%**	**1.2%**	**11.8%**	**2.5%**	**9.6%**	**7.4%**	**7.4%**
	5 Year Average (2018-2022)	**5.3%**							

A Short Note on Volatility

The past 2 years there has been a meaningful structural shift at Fairfax in total investment return towards what are considered higher quality sources.

From 2018-2022, two items, interest and dividends and share of profit of associates, represented 48% of the total investment return each year. In 2024, the same two items now represent 66% of the estimated total investment return. It is the same (66%) for 2025.

Bottom line, there should be significantly less volatility in Fairfax's total investment return moving forward when compared the past. For most investors lower volatility = higher quality. And higher quality earnings deserve a higher multiple (P/BV).

What does Fairfax's historical P/BV look like?

Fairfax's stock trading today at a P/BV multiple of 1.1 x; this looks to be near the lower end of its historical range. Does this make sense given what we know about the company today?

Source: COBF @MMInvestor0

What is the quality of Fairfax's equity portfolio?

April 3, 2024

In the previous post I asked a question: What is the quality of Fairfax's equity portfolio?

My thesis is as follows: Fairfax's equity holdings (as a group) have materially improved in quality over the past 6 years. And I don't think this fact is yet fully recognized by investors today. Moving forward, this could continue to be an important tailwind to earnings.

This is the topic we will explore in this post.

Now I know for some investors, reading the words 'quality' and 'equity portfolio' and 'Fairfax' all in the same sentence will cause them to laugh uncontrollably out loud. If this is you, try and keep an open mind.

I also would appreciate hearing what board members think about this post. Sometimes I get an idea and I have a hard time explaining it (which usually means it is still all jumbled up in my head). So, like spaghetti, I throw it against the proverbial wall at COBF, and see what sticks. The feedback received from other board members helps me flesh out ideas. Am I on to something important? Or am I out to lunch?

Let's start with the big picture.

<u>A quick review: The 3 drivers of earning at Fairfax</u>

- Insurance + fixed income investments + equity investments = earnings

- Earnings feeds ROE, which feeds into the multiple, which feeds into the stock price.

The important take-away for this post: the return on the equity investments is one of the key drivers of Fairfax's stock price.

Of interest, most investors today likely own Fairfax to get exposure to its insurance business and its fixed income portfolio. Its equity portfolio? Woof! (Not so much.)

20 years ago, investors owned Fairfax to get exposure to its equity and fixed income portfolios. Insurance? Woof!

How the narrative at Fairfax has changed. But what if the current narrative attached to the equity portfolio is wrong?

<u>Why do we care about the 'quality' of the equity portfolio?</u>

The 'quality' of Fairfax's equity portfolio will impact two things:

- The return achieved over time
- The volatility of the return

Today investor's view Fairfax's equity portfolio as being of low quality (overall). And they think it is highly volatile. That is what is built into Fairfax's stock price today.

But what if both of these assumptions are wrong?

What if Fairfax's equity portfolio can be characterized as being 'high quality' today? And what if it also has lower volatility moving forward than in the past?

If true, this means investors are likely underestimating both the earnings potential of Fairfax and the multiple those earnings deserve (which is tied to volatility).

<u>How are we going to measure the quality of Fairfax's equity portfolio?</u>

Let's open this big can of worms.

There is no standard definition of 'quality' that can be applied to all companies and industries - this is because every investor has their own definition. The problem with this type of analysis is most people come at it in a subjective way. Not an objective way. So discussing it with others can be like trying wrestle with a greasy pig.

How do we remove our own biases from our assessment? Of course, we can’t. Most people don’t even want to. We all have our own investing framework - it’s what allows us to function as investors. And it’s the prism we use when we evaluate the management team at Fairfax.

When we look at a stock that Fairfax owns and we comment ‘good’ or ‘bad’ - well, often we are telling others more about our own mental model than about the actual holding or the management team at Fairfax.

<u>What about volatility?</u>

We can’t really answer the ‘quality’ question without also discussing volatility.

Current finance theory states: low volatility = high quality. Potential return matters less.

We are going to look to Warren Buffett for guidance on this topic.

> “Gyrations in Berkshire's earnings don't bother us in the least: Charlie and I would much rather earn a lumpy 15% over time than a smooth 12%.” *Warren Buffett BH 1996AR*

From our perspective, if volatility can be reasonably expected to deliver a higher rate of return over time, then we can ignore it from the quality discussion.

Let’s circle back to our objective.

<u>What methodology are we going to use in our analysis?</u>

There are a couple of different methods we can use to help us answer the ‘quality’ question:

1. Quantitative - top down/follow the money - focus on the total return being delivered by the equity holdings (as a group).
2. Qualitative/quantitative - bottom up - look at each of the individual holdings and sum our findings into a total.

<u>Quantitative - top down - measure of quality</u>

> “For a value investor, price has to be the starting point. It has been demonstrated time and time again that no asset is so good that it can’t become a bad investment if bought at too high a price. And there are few assets so bad that they can’t be a good investment when bought cheap enough.”
> *Howard Marks*

> “Price is what you pay. Value is what you get.” *Warren Buffett*

Fairfax has stated they have a pre-tax return target for their equity investments of 15%.

Can we use this target as a core input into our 'quality' measure?

I think we can.

I come at the quality discussion in a very simple and selfish way. As an investor in Fairfax, when looking at the equity portfolio (in aggregate), what I want to know is 'will it deliver a return of 15% per year on average over the next couple of years?'

If the equity portfolio has a good chance of delivering a pre-tax return of:

- 15% per year = high quality
- 10% per year = average quality
- 5% per year = below average quality
- Negative return = dog with fleas

Do I really care what Fairfax owns? I kind of do.

But what I care about much more is whether or not their portfolio of holdings can hit the stated 15% target.

<u>What return would the equity portfolio have to deliver to hit 15%?</u>

This number is easy to calculate. The equity portfolio had a market value of about $19 billion at March 31, 2023. (This uses carrying value. And values the FFH-TRS at its notional value).

- $19 billion x 15% = $2.85 billion

<u>Can Fairfax's equity holdings deliver a pre-tax return of $2.85 billion in 2024?</u>

We have already done this work. It is contained in our earnings estimate for 2024.

What do the numbers say?

- Dividends = $170 million
- Share of profit of associates = $1.03 billion
- Other / Non-insurance consolidated holdings = $150 million
- Mark to market investment gains = $1 billion
- Realized one-time investment gains = $300 million
- Change in excess of fair value over carrying value for associate and consolidated holdings = $200 million
- Total = $2.85 billion

Of course, the 6 buckets above do not capture everything. Especially for non-insurance consolidated holdings. And I also cheated a little - I include both insurance and non-insurance holdings when estimating 'realized one-time investment gains'. But I think my estimate is directionally accurate.

Bottom line, my current earnings forecast has Fairfax generating a return of about 15% from its equity holdings in 2024. My guess is this comes as a surprise for most Fairfax shareholders.

Based on our quantitative framework, can we conclude that Fairfax's equity portfolio is high quality? Yes, I think we can.

Let's now see what our second measure says.

Qualitative/quantitative - bottom up - measure of quality

Let's pivot with our analysis and now look at the individual holdings to see what we can learn. The 80-20 rule applies here. The big holdings are the key - if they perform well then Fairfax's total return for the equity portfolio will likely be good.

Context is also important. How did things look in 2017? How do things look today? Is the trend getting better? If so, how much better?

What are some questions we would want to ask when evaluating the individual holdings?

To help answer the 'quality' question when looking at the individual holdings, here are a few questions that come to mind:

- How good is the management team? Capital allocation?
- Is the balance sheet in good shape? Leverage?
- Is the company profitable? Is growth funded via retained earnings?
- What are the future prospects of the business?
- Other considerations (geography, political/economic situation etc)?
- What has Fairfax's return been since purchase?
- What is Fairfax's return potential looking forward?

Back in 2017, Fairfax had a number of large holdings that could be described as follows:

- Poorly managed.
- Stressed balance sheets.
- Not profitable.
- Poor future prospects.
- Past returns for Fairfax were poor.
- Future return potential for Fairfax was poor.

Fast forward to 2024 and it is amazing the turnaround that has been executed by the team at Hamblin Watsa. Over the past 6 years the equity portfolio has seen a complete make-over. The many problems have largely been fixed (run-off, sold, restructured, merged). And capital allocation has been outstanding (new position purchased, buying more of existing positions etc).

Let's look at Fairfax's top 15 equity holdings:

Fairfax has a pretty concentrated equity portfolio. The top 15 positions represent 67% (2/3) of the total portfolio.

Fairfax - Equity Holdings Ranked by Size			Estimated			Dec 31 '23
March 31, 2024 (US$ millions)			Market			Carrying
Rank	Ticker	Holding	Value	Weight		Value
1	EUROB.AT	Eurobank	$2,436	12.7%		$2,099
2	FRFHF	Fairfax - TRSwaps	$2,119	11.1%	Top 3	
3	Private	Poseidon	$2,046	10.7%	34.5%	$1,706
4	FIH-U.TO	Fairfax India	$860	4.5%		$758
5	Private	Recipe	$684	3.6%		$684
6	Private	BDT Capital Partners	$683	3.6%		
7	THOMASCO(	Thomas Cook India	$599	3.1%		$201
8	Private	Grivalia Hospitality	$567	3.0%		$567
9	Private	ShawKwei & Partners	$504	2.6%	Top 10	
10	MU	Micron Tech	$461	2.4%	57.3%	
11	Private	EXCO Resources	$435	2.3%		$418
12	STLC.TO	Stelco	$429	2.2%		$292
13	EGS60121C0	Com Int Bank - Egypt	$362	1.9%		
14	OXY	Occidental Petroleum	$357	1.9%	Top 15	
15	MYTIL.AT	Mytilineos *	$355	1.9%	67.4%	
		Remainder	$6,229	33%		
		Total	**$19,127**			

1.) Eurobank

Fairfax's biggest holding today - by far - is Eurobank. It is also the best example of the renaissance that has happened in Fairfax's equity portfolio over the past 6 years.

Back in 2017, Greece was ruled by a far left government and its economy was a mess. Eurobank's balance sheet was not good (lots of non-performing loans).

But look at the transformation that has happened since:

- In 2019, Greece elected a center/right government who got to work reforming the Greek economy.
- Fairfax merged Grivalia Properties with Eurobank to improve its capital position.
- Eurobank's management team has always been solid - they aggressively shed non-performing loans and shifted capital from Serbia (selling their operations there) to Cypress (buying Hellenic Bank).
- Greece just re-elected the center/right government so the pro-business reforms to the economy will continue. Greece is expected to have one of the top performing economies in Europe in the coming years.
- Bottom line, Eurobank is very well positioned today.

Was Eurobank a quality holding back in 2017? No. It and Greece were turnarounds with an unknown future. Is Eurobank a higher quality holding today than it was in 2017? The answer is an unambiguous yes. And we see this in the return it is delivering to Fairfax.

My guess is Eurobank was not earning much money back in 2017. Today? My current forecast is Eurobank will deliver $440 million in share of profit of associates to Fairfax in 2024. Fairfax's carrying value for Eurobank was $2.1 billion at December 31, 2023. This would deliver a return of 21% to Fairfax. Outstanding.

2.) Fairfax - Total Return Swap

Fairfax's second largest equity holding is the FFH-TRS. I include this holding in the 'equity' bucket. This holding did not exist is 2017. Fairfax did exit their equity hedge position in late 2016. But in 2017, Fairfax still had significant short positions in place on individual stocks. These positions were not closed out until 2020 and lost about $1 billion in total from 2017-2020.

The 'swing' here is enormous - losing $1 billion shorting something you clearly didn't understand very well - to making +$1 billion on something you understand exceptionally well (your own company). This has been great swing trade for Fairfax and its shareholders.

At December 31, 2023 the FFH-TRS position was valued at $1.8 billion. My current forecast is this investment will deliver gains of $500 million in 2024 ($250/share x 1.96 million shares). This would deliver a return of 28% to Fairfax.

3.) Poseidon

Of all of Fairfax's largest holdings, Poseidon was the biggest disappointment for me in 2023. The spike in interest rates seemed to catch management at Poseidon flat footed - and thrown a wrench into expected profit growth. Was 2023 the low point for earnings? 2024 will be an important year for Poseidon.

My current forecast is Poseidon will deliver $180 million in share of profit of associates to Fairfax in 2024. Fairfax's carrying value for Poseidon was $1.7 billion at December 31, 2023. This would deliver a return of 10.5% to Fairfax. While below the hurdle rate of 15%, this return is far from being a catastrophe. And it is expected to improve in the coming years.

> "Poseidon is expected to make net earnings in excess of $400 million in 2024 and $500 million in 2025. We carry our 43% ownership in Poseidon at $1.7 billion – 10x 2024 expected earnings or 8x 2025 expected earnings." *Fairfax 2023AR*

4.) Fairfax India

The key to this holding is BIAL. Is BIAL a higher quality asset today than it was in 2017? The answer is an unambiguous 'yes'. What BIAL has accomplished over the past 6 years is amazing. It added a second runway and a second terminal. It is perfectly positioned to grow rapidly in the coming years - the runway is long. The management team in place is very good.

In 2017, Fairfax owned 48% of BIAL - it did not yet have a control position. Today, Fairfax India owns 64% of BIAL (not adjusting for Anchorage), putting it firmly in control. Today, Fairfax also owns significantly more of Fairfax India (42%) than it did in 2017 (30%).

Modi appears he will be re-elected to a third consecutive term in India. This should cement India's economic pivot away from a socialist/Soviet model to a more capitalist model. Global capital is exiting China with India being a big beneficiary. India is projected to be the top performing economy in the world over the next decade and Fairfax India is well positioned to benefit from this strong tailwind.

Fairfax's carrying value for Fairfax India is comically low $768 million. A 15% return for Fairfax = $114 million. That is a lay-up.

5.) Recipe

I have been highly critical of Recipe in the past. Minority shareholders were used like a piggy bank to fund its aggressive and flawed roll-up of restaurant chains in Canada. However, there is a decent business there. Covid was a gut punch - it hit dine-in full service restaurants in Canada especially hard. Spiking inflation, taxes and minimum wages threw more sand in the wheels.

Bottom line, Recipe needed to restructure its operations. It got the process started back in 2021 - poorly performing locations/franchisees were closed and debt levels were materially reduced. But that is a hard thing to do as a publicly traded company. In 2022 Fairfax took Recipe private. Fairfax got a great price. And Recipe got the ability to complete its restructuring out of the public/shareholder spotlight.

Fairfax's carrying value for Recipe was $684 million at December 31, 2023. Free cash flow was US$92 million (C$125 million) in 2023 - back to pre-pandemic levels.

Price paid matters a lot. Fairfax was able to take Recipe private at a very good price. The company is delivering a solid return to Fairfax.

"Recipe, operating in its first full normal year since the pandemic, achieved record system sales in 2023. Sales increased to Cdn$3.7 billion, up 9% from 2022 and 5.6% higher than 2019. Margins also increased by 20 basis points, or 15% in dollars terms, over 2022. Impressively, the company delivered over Cdn$150 million in free cash flow and reduced overall leverage to less than 2.5x. Frank Hennessey, Ken Grondin and his team are focused on continuing to improve the overall margin rate while emphasizing top line growth. Expansion is underway in the United States and India markets as well as organic growth in Canada driven by new restaurants. The company will also be launching new products in its already sizable consumer packaged goods business (where Recipe's brands are sold in grocery stores). Recipe is carried at 8x enterprise value to EBITDA on our balance sheet or 10x free cash flow." *Fairfax 2023AR*

The next 5 holdings

6.) BDT Capital Partners (private) - this has been an outstanding long-term holding for Fairfax.

Who are they? "BDT & MSD Partners is a merchant bank with an advisory and investment platform built to serve the distinct needs of business owners and strategic, long-term investors. We are distinguished by our decades of experience advising at the intersection of founders, families, and businesses, as well as by our differentiated capital base and culture of aligned investing." https://bdtmsd.com

> "We continue to invest with Byron Trott through various BDT Capital Funds. Since 2009, we have invested $978 million, have received $979 million in distributions and still have investments with a year-end market value of $683 million. Byron and his team have generated fantastic long-term returns for Fairfax, and we very much look forward to our continued partnership." *Fairfax 2023AR*

7.) Thomas Cook India (public) - management implemented an aggressive cost cutting plan during Covid. In 2023, people in India started travelling again and revenue at TCIC spiked higher. With a structurally lower cost base, profits have surged. TCIC was a star performer for Fairfax in 2023 - its stock has increased 140% over the past 15 months.

> "Thomas Cook's business rebounded in 2023 as travel recovered, with revenues up and a pre-tax profit of $34 million, up from a loss of $2 million last year. Thomas Cook stock price was up 90% in the Indian stock market in 2023. We sold 40 million shares at $1.67 to repay the $60 million we invested last year in the company. Future prospects for Thomas Cook look excellent in the years to come." *Fairfax 2023AR*

8.) Grivalia Hospitality (private) - this holding gets an 'incomplete' from me today. It is a bet on the jockey. George Chryssikos has had the Midas touch for Fairfax in Greece - making them +$1 billion so far. I am inclined to give Fairfax the benefit of the doubt on this one - my guess is it works out ok. We should know much more in 2024 as more resorts come on line.

> "Grivalia Hospitality, under George Chryssikos, had a strong year of execution as two assets, including its largest, opened for business. The One & Only resort in Athens is a flagship in ultra-luxury hospitality and we are the proud owners. If you haven't booked your summer vacation yet – you know what to do! 2024 will see one additional asset come into operation – which will take the operating portfolio to five. These include Amanzoe in Porto Heli, ON Residence in Thessaloniki, Avant Mar in Paros, One & Only and 91 Athens Riviera in Athens. Focus now turns to operational and service excellence for these resorts with Greece forecast to receive a record number of tourists in 2024. George has another five high end hotels in development over the next few years. George has an outstanding track record in real estate and as I said last year, he has already made us $1 billion! We expect George to repeat that accomplishment with Grivalia Hospitality over time! At year end we carried Grivalia at €513 million for our 85% stake." *Fairfax 2023AR*

9.) ShawKwei & Partners (private) - this holding has been a solid long-term performer for Fairfax. The fact Fairfax is adding new capital suggests they like the prospects.

> "Since 2008 we have invested with founder Kyle Shaw and his private equity firm ShawKwei & Partners. ShawKwei takes significant stakes in middle-market industrial, manufacturing and service companies across Asia, partnering with management to improve their businesses. We have invested $536 million in two funds (with a commitment to invest an additional $64 million), have received cash distributions of $217 million and have a remaining value of $504 million at year-end. The returns to date are primarily from our investment in the 2010 vintage fund, which, though decreasing 8.8% in value in 2023, has generated a 12% compound annual return since 2010. The 2017 vintage fund, which has drawn about 84% of committed capital to date, increased 23.1% in value in 2023 but has a compound annual return of 3.5% since inception. We expect Kyle to make higher returns on monetization of his major assets." *Fairfax 2023AR*

10.) Micron Technologies (public) - Fairfax materially increased their position in Micron in Q3 of 2022; likely around $60/share. The stock closed today at $128/share so Fairfax is likely up about 100% on its position in less than 2 years. Outstanding.

The next 5 holdings

11.) EXCO Resources (private): This holding has been a solid performer for Fairfax in recent years. Consolidation seems to be a big trend in oil and gas. My guess is the company gets taken out at some point in the next year or two.

> "In 2023, Exco Resources (a U.S. oil and gas producer) repurchased 8% of its shares. This increased Fairfax's ownership of Exco from 44% to 48%. After year end, Exco repurchased another 2% of its shares, increasing our ownership to 49%. Both transactions occurred at steep discounts to intrinsic value. Sometimes, as T. Boone Pickens noted, "it is cheaper to drill for oil (and gas!!) on the stock exchange than it is to drill directly". Of course, Exco also did plenty of drilling. In 2023, Exco added more than twice as much to its reserves as it extracted through production. With weakness in commodity prices, the present value of proved reserves dropped. However, production volumes increased 3.2% year over year. Exco is well-positioned to navigate commodity price volatility. It has a strong balance sheet, nimble operations and decisive leadership. Chairman John Wilder and CEO Hal Hickey lead Exco. Fairfax's Wendy Teramoto and Peter Furlan are on its Board. Fairfax is well served by our long-term partners, John and Hal, who transformed Exco into a resilient oil and gas company. Exco is carried on our balance sheet at $418 million or $18.24 per share, approximately 3x net income in 2023, an increase from $12.59 per share last year, due to our share of their 2023 earnings of $5.65 per share." *Fairfax 2023AR*

12.) Stelco (public): In late 2018, Fairfax paid $193 million for 14.7% of Stelco. Since then Stelco has paid Fairfax $106 million in dividends. Over the past 3 years Stelco has also repurchased 38% of all shares outstanding - so Fairfax now owns 23.6% of Stelco. The CEO of Stelco, Alan Kestenbaum, is a rock star - even Billy Idol would agree. When the next bull market hits the steel market, Stelco and Fairfax are going to make an absolute killing; remember, Fairfax now owns 23.6% of the company. There is also a good chance Stelco gets taken out at a premium valuation by a bigger player.

When Fairfax announced their Stelco purchase in late 2018 I hated it. At the time, it screamed 'old Fairfax' to me. Boy was I wrong. But I have since updated my view of the holding and I love it today. Facts are facts.

But talk to Fairfax detractors - and my guess is they still view Stelco as a shitty investment. It is a commodity producer after all! It cracks me up when I hear the detractors talk about Fairfax's equity holdings. They usually have no idea what they are talking about. But boy do they ever have a lot of conviction when they express their views.

"In a year of volatile steel prices, Stelco performed well, highlighting its competitive cost structure. Stelco's talented team – led by Alan Kestenbaum, Sujit Sanyal, and Paul Scherzer – continues to be excellent stewards of the business with a keen focus on creating shareholder value. We believe that Stelco owns the best-in-class blast furnace assets in North America, which is highlighted by its industry leading margins. The company's Lake Erie Works facility has had recent upgrades to its blast furnace, coke battery, a newly constructed co-generation facility and a new pig iron caster. Nippon recently announced an agreement to acquire US Steel at a multiple of 7.8x 2024 EBITDA, a significant premium to Stelco's trading multiple. We believe the US Steel acquisition highlights the value of blast furnace operations. Stelco continues to have significant net cash on its balance sheet, providing management with flexibility to take advantage of both organic and inorganic growth opportunities. The company rewarded shareholders with a Cdn$3 per share special dividend in addition to its Cdn$1.68 per share regular dividend in 2023. Stelco has raised its regular dividend for 2024 to Cdn$2.00 per share. We believe Stelco has a bright future under Alan Kestenbaum's leadership. Stelco is carried on our books at $22.44 per share versus a market price of $37.84 per share." *Fairfax 2023AR*

<u>13.) Commercial International Bank (public)</u>: This is a very well run bank. Unfortunately, perpetual currency devaluations in Egypt have made this a tough investment for Fairfax. Fairfax invested $330 million in 2014. As of March 31, 2024, their position was valued at $362 million. Over the past decade, the opportunity cost to Fairfax from this investment has been significant. This holding is one of the last 'old Fairfax' positions remaining at Fairfax (that is a decent size).

"Commercial International Bank (CIB) results were very strong in 2023 with an ROE of over 40%, net interest margin of almost 8% and loan-loss provision coverage ratio of approximately 230%. There is significant hidden value in the build-up of provisions on the balance sheet which if adjusted for, reduces the price-to-book ratio well below 2x. Since 2014, the bank has continued to compound book value per share and EPS by nearly 20% per annum. The key driver of value to Fairfax and other foreign investors in CIB is the stability of the Egyptian Pound. Fairfax invested the vast majority of its position in CIB in the spring of 2014 when the market cap was less than $5 billion, at exchange rates at the time. During that same time, net profit at CIB in USD terms (at current exchange rates) has more than doubled and the market cap stands at just $7 billion with an estimated 2024 price to earnings ratio of 6x. By comparison, in local currency, the market cap has increased over five times! The Egyptian government has begun a massive asset disposal program to address the country's high sovereign debt. Execution will be critical to ensure foreign investors more than just tread water on their investments. Hisham Ezz Al-Arab, the Founder of the modern CIB Bank, came back as Chairman in December 2022." *Fairfax 2023AR*

14.) Occidental Petroleum (public): Initiated in 2022, this is a relatively new position for Fairfax. They increased it meaningfully in 2023. Their average cost is likely around $60/share. Stock closed today at $67. This holding looks well positioned. And it has Warren Buffett's seal of approval.

15.) Mytilineos (public): a global industrial and energy company covering two business Sectors: Energy and Metallurgy. Fairfax initiated their position in Mytilineos in 2012. They more than doubled their position in late 2022 at €18.50/share. Shares closed today at €34. This has turned into another outstanding investment for Fairfax.

Summary

After all that what have we learned?

Can we conclude that Fairfax's collection of equity holdings is higher quality than what they were in 2017? Yes, I think we can. And by a lot.

Fairfax has been hard at work the past 6 years improving the overall quality of its basket of equity holdings. It takes years for that work to show up in reported results. And that is what we are now seeing. We are just now starting to learn what the true earnings power of the equity portfolio is today.

Can we also call the collective holdings 'high quality'? Given they look poised to deliver a 15% return, yes, I think we can.

And my guess is Fairfax is not done with its move up the quality ladder with its collection of equity holdings. This bodes well for higher future returns.

Total Return on Investment Portfolio:

- Fixed income yield = 4.7%
- Equity return = 15%
- Total return on investment portfolio = 7.4%

What about further out - a couple of years into the future? That will depend on the capital allocation decisions that are made. If Fairfax continues to make good capital allocation decisions i don't see why total return on the investment portfolio can't stay in the 7.5% range for the next 5 years.

Is that baked into the expectations of investors today? No, I don't think it is.

The Drivers of a share price – Earnings, Multiple and Share Count

February 2, 2024

Three things drive a share price:

1. Earnings
2. Multiple
3. Share count

In buying a stock, an investor is buying a stream of future earnings. The multiple is simply the price an investor is willing to pay for the stream of future earnings. These are called fundamentals.

Understanding the change in each of these items gives an investor great insight into the future path of a stock. It's like being able to predict the future.

Of course, the perfect set-up for an investor is to find a company that is:

1. Growing earnings
2. Experiencing multiple expansion
3. Reducing its share count

Finding a company where one of these things is happening is usually pretty good. Finding a company where two are happening at the same time - that usually leads to market-beating returns. Finding a company where all three things are happening at the same time - well, that is how the big money is made - or multi-baggers in Peter Lynch parlance.

Theory is great. But is it actually possible for an investor to find a stock that is poised to do all three at the same time? Aren't markets supposed to be pretty efficient?

Well grasshopper, let's pivot to the real world and look at an unloved, scrappy P/C insurance company called Fairfax Financial. Yes, it is still unloved... we will show you why in this post.

<u>A real life example: Fairfax Financial</u>

<u>Buybacks</u>

Let's start with share buybacks because they are the easiest.

Over the last 4.75 years Fairfax has spent $1.94 billion and reduced effective shares outstanding by 4.12 million or a total of 15.1% (3.2% per year). This is a material reduction in share count. The average cost was $470/share. With shares closing Friday at $1,030, the shares were purchases at an average cost well below their intrinsic value. This is an example of great capital allocation on the part of management at Fairfax. Share count has been materially coming down for the last 4.75 years at Fairfax.

We can check off box three from our list above.

Fairfax - Reduction In Effective Shares Outstanding - Last 4.75 Years				
	Shares	Change		
Year End	Dec 31	Shares	%	Comments (US$)
2018	27,237,947	n/a	n/a	
2019	26,831,069	-406,878	-1.5%	Avg price = $464/share
2020	26,176,506	-654,563	-2.4%	Avg price = $298/share
2021	23,865,600	-2,310,906	-8.8%	Avg price = $490/share
2022	23,325,305	-540,295	-2.3%	Avg price = $509/share
Sept 30 2023	23,115,838	-209,467	-0.9%	9 Month avg price = $698/share (Sept 30)
Total decline in shares		-4,122,109	-15.1%	2018 to Sept 2023. Avg price = $470/share
Average annual decline		-867,812	-3.2%	4.75 year average decrease

Earnings

Let's move now to earnings. Earnings at Fairfax have spiked over the past 3 years. And because of the significant reduction in shares, per share earnings are up even more.

When analyzing P/C insurance companies, analysts prefer to look at operating income. It removes the volatility tied to 'icky' investment gains. Ok, let's play be their rules and only look at the 'good stuff' - operating income.

Operating income at Fairfax averaged $1 billion ($39/share) per year for the 5-year period from 2016-2020. Over the next 3 years (2021-2023) it was like a goat going straight up a mountain. For 2023 my estimate is operating earnings will come in around $4.4 billion ($190/share). This is a 387% increase per share. My forecast is for operating income to come in around $4.6 billion ($202/share) in 2024. This higher level is durable and growing. Bottom line, we are seeing a significant increase in earnings at Fairfax.

We can check off box 1 from our list above.

Fairfax - Operating Income									
December 31, 2023	2016	2017	2018	2019	2020	2021	2022	2023E	2024E
Underwriting profit - ins & reins.	$576	-$642	$319	$395	$309	$801	$1,105	$1,373	$1,270
Interest & dividends	$555	$559	$784	$880	$769	$641	$962	$1,929	$2,250
Share of profit of associates	$24	$201	$221	$170	-$113	$402	$1,015	$1,100	$1,100
Operating income - ins & reins	**$1,155**	**$118**	**$1,323**	**$1,444**	**$965**	**$1,844**	**$3,082**	**$4,402**	**$4,620**
Per share	$50	$4	$49	$54	$37	$77	$132	$190	$202
Shares Outstanding Dec 31	23.1	27.75	27.2	26.8	26.2	23.9	23.3	23.2	22.9

Multiple

What about multiple?

Share count and earnings are relatively easy to understand - they are largely based on numbers.

Multiple can be a more difficult nut to crack. Yes, it is based on numbers. But it is also steeped in psychology. To give multiple the attention it deserves we are going to write about it in a separate post.

Multiple expansion - a deep dive

In this post, we will do a deep dive on multiple to see what we can learn. First, we will zoom out and look at the big picture. And then we will zoom in and apply what we have learned to Fairfax.

This post is broken into the following parts:

- Part 1 - Multiple
- Part 2 - Turnarounds
- Part 3 - The turnaround is complete - the caterpillar has transformed into a butterfly
- Part 4 - Narrative change and multiple expansion
- Part 5 - Multiple expansion - What does the math look like?
- Appendix - Is growth in book value a good measure of quality?

<u>Part 1 - Multiple</u>

What is the multiple for a stock?

A multiple is a quick and easy way to value a company. It is best used to compare valuations of companies in the same industry.

A low multiple (when compared to peers) suggests a stock may be undervalued - a high multiple suggests the opposite.

<u>What determines the multiple a stock trades at?</u>

Two things primarily drive the multiple:

1. <u>Past results and events</u>. The facts.

We all know the axiom: "The best predictor of future behaviour is past behaviour." Well, it appears the same holds true for financial results.

2. <u>Narrative</u>. This is 'the story,' or how the facts have been interpreted. A large part of narrative is driven by psychology.

Most companies are pretty predictable animals. They tend to have the management team. Future earnings tend to follow in an arc consistent with their historical trend. A narrative - that is reasonably accurate - settles in over time for most companies. And it tends to remain largely the same, sometimes for decades.

As a result, most companies tend to trade at a pretty stable multiple over the years (within a stable band).

Let's steer this discussion back to Fairfax. To do this we need to bring turnarounds into the picture.

<u>Part 2 - Turnarounds</u>

As part of his investment framework, Peter Lynch classified all stocks into six broad categories - one of which was turnarounds.

With turnarounds, past results/events usually have been pretty bad. This usually results in a narrative that is quite negative. Lower earnings and a poor narrative tend to compress the multiple - often to extremes. This set-up usually causes the share price to crater.

<u>Why did Lynch like turnaround plays so much?</u>

Lynch loved turnarounds because of their potential to become big winners - sometimes 5 and even 10 baggers. Another benefit is the returns are usually not correlated with the overall market.

<u>Why are successful turnarounds so lucrative for investors?</u>

When investing, your starting point matters. Buy low. The stocks of lots of turnaround plays have been left for dead by investors - often you can buy them at crazy low prices.

For successful turnarounds, two things happen. But usually along two very different time-frames:

1. Short term (1 to 2 years): earnings turn.
2. Medium term (3 plus years): multiple expansion.

Of course, higher earnings tend to lead to a higher stock price. Facts are facts.

But multiple expansion? This usually takes years to happen.

Why?

The multiple is largely driven by the looking through the rear view mirror - a narrative that has been constructed from past events.

For successful turnarounds it often takes years for the narrative to get updated.

Why does it take so long?

There are a couple of reasons.

1. Most turnarounds are under-followed. For the most part these are companies that have disappointed investors for years. Analysts? Investment professionals? Losing your clients money year after year by recommending a shitty stock is never a good career move. As a result, most turnarounds become hated companies.

Lack of coverage results in an information disadvantage. Of course, some turnarounds actually turn around. And guess what? Pretty much no one notices - because no one is following the company anymore. And if no one is following the company it is impossible for the old narrative to change - even after the fundamentals have turned.

2. There is a second reason it takes a long time for narratives to change and it is very powerful. **Holding on to an old (wrong) narrative requires no work.** After all, people are busy.

Updating a narrative? Now that is hard. It requires a lot of work. And in the beginning almost everyone around you is going to think you are an idiot.

But over time (sometimes years in length), as it becomes obvious to more and more people that the turnaround has actually happened, the 'story' around a stock gets to an inflection point. And those clinging to the old narrative are the ones who start to sound like idiots. And do you want that 'crazy uncle' managing your money? (Darwin at work on Bay and Wall Street.)

Eventually, the narrative does get updated. And as that happens, we see multiple expansion.

<u>So, what does all this have to do with Fairfax?</u>

Fairfax is a turnaround play. That has turned around. It actually started to turn around all the way back in late 2016 when it removed all the equity hedges (Trump getting elected was a great event for Fairfax shareholders). It picked up steam in 2018 and 2019 when the company got to work fixing its poor quality equity portfolio. We probably could say the turnaround was largely done at the end of 2020 when Fairfax covered its last short position.

For sure, the turnaround was done by the end of 2021 - that is when all the positive changes from the previous years started to show up in much higher (record) operating income.

Bottom line, the turnaround at Fairfax was completed years ago. Yes, I know… shocker!

Fairfax has transformed itself over the past 6 years into a high quality insurance company. And that matters a lot when it comes to multiple. This is what we are going to explore next.

<u>Part 3 - The turnaround is complete - the caterpillar has transformed into a butterfly</u>

How do we know Fairfax has transformed itself into a high quality insurance company?

To help us answer this question we are going to look at something called return on equity (ROE).

Return on equity (ROE)

Return on equity is a measure of how profitable a company is. The bigger the number - the higher the quality.

We are also going to look at operating income ROE (which I will call OI-ROE). This is viewed by the P/C industry as being a higher quality measure of ROE.

Operating Income ROE at Fairfax

- For the 5-year period from 2016-2020, the OI-ROE averaged 9%.
- For the 3-year period from 2021-2023, the OI-ROE averaged 19%.
- My estimate for 2024 is 20%.

OI-ROE has doubled from 9% to 19%. That is a massive increase.

OI-ROE of 20% is top-tier performance among P/C insurers. Fairfax is tracking in 2024 to deliver its 4th year in this range. That is exceptional performance and a material increase from what it delivered in the past.

Fairfax - Operating Income									
December 31, 2023	**2016**	**2017**	**2018**	**2019**	**2020**	**2021**	**2022**	**2023E**	**2024E**
Underwriting profit - ins & reins.	$576	-$642	$319	$395	$309	$801	$1,105	$1,373	$1,270
Interest & dividends	$555	$559	$784	$880	$769	$641	$962	$1,929	$2,250
Share of profit of associates	$24	$201	$221	$170	-$113	$402	$1,015	$1,100	$1,100
Operating income - ins & reins	**$1,155**	**$118**	**$1,323**	**$1,444**	**$965**	**$1,844**	**$3,082**	**$4,402**	**$4,620**
Per share	$50	$4	$49	$54	$37	$77	$132	$190	$202
Shares Outstanding Dec 31	23.1	27.75	27.2	26.8	26.2	23.9	23.3	23.2	22.9
Operating Income ROE	13%	1%	11%	12%	8%	14%	21%	24%	20%
E = average equity	5-Year Average (2016-2020) = 8.9%					3-Yr Avg (2021-2023E) = 19.5%			

I can hear the naysayers yell out as they are reading this post… "Ya, but it's not sustainable!"

To which I would answer: 3 years in a row at an average OI-ROE of 19.5% is in the books (well, should be when Fairfax reports Q4 results). A 4th year at 20% looks likely. Is 4 years in a row not the beginning of a trend? Maybe not 20%. But even something in the high teens range over the next 5 years would put Fairfax among the top tier of P/C insurers.

I could also bring up investment gains. This is something we have completely ignored but is a clear strength of Fairfax (when compared to peers). Pet insurance? Sold in 2022 for a $1 billion after-tax profit. The FFH-TRS position (providing exposure to 1.96 million Fairfax shares) is up $1.3 billion (pre-tax) over the past 37 months. I could go on. Volatile? Yes. But smoothed out over a few years, the average number is a significant contributor to Fairfax's regular ROE calculation. Just something to keep in mind.

But to help us answer the question of whether or not the high OI-ROE is sustainable, let's peel the onion back one more layer.

What is the best predictor of long term results for a company?

The best predictor of long term results for a company is the management team and their capital allocation skills. This is especially true for P/C insurance companies because of something called float (which can be larger in size than shareholder's equity).

The quality of the capital allocation decisions being made by management is likely the best leading indicator for future ROE for a P/C insurer.

Of course, it takes years for good capital allocation decisions to show up in higher earnings and higher ROE. Especially for a turnaround like Fairfax. But that is exactly what we have been seeing in each of the past three years.

But the story gets better. I wrote a very long post last week where I went into great detail on Fairfax's capital allocation record over the past 6 years or so. The conclusion? Fairfax looks best-in-class in the P/C industry.

If you have one of the best capital allocation teams in the industry, and they have been hitting the ball like Ted Williams over the past 6 years, what do you think ROE will look like in the coming years? Above average for sure. And probably even better than that.

As a result, I think the facts and evidence points to Fairfax being a high quality insurance company.

How is Mr. Market valuing Fairfax? Finally, we get to our answer!

ROE and P/BV

Return on equity (ROE) and price to book value (P/BV) are the preferred metrics used by investors to value P/C insurance companies. Looked at together, they tell investors a story about the company.

Over time, a high and sustainable ROE inevitably results in a high P/BV multiple. The opposite is also true: a low ROE generates a low P/BV multiple.

Return on equity

Earlier we learned that OI-ROE at Fairfax is tracking to overage 20% from 2021-2024. That is top tier performance.

Let's now compare that to P/BV.

Price to book value (P/BV)

This measure tells us what Mr. Market thinks about the future prospects of the company. Or put another way, is ROE sustainable?

Fairfax's P/BV is about 1.11 (if we use estimated 2023 YE book value). Compared to peers, Fairfax's P/BV is at the very bottom. A P/BV near 1 suggests the P/C insurer is both poorly run and has poor prospects.

Fairfax has a very high ROE (with solid prospects). The company is high quality.

Yet, its P/BV multiple is very low. This suggests Fairfax is very undervalued.

Fairfax (US$)		
Share Price	$1,031	Feb 2, 2024
Book Value *	$932	Est Dec 31, 2023
P/BV	1.11	
ROE (average equity)**	20%	
BV* = $877 + $55 (Yahoo Finance Q4 est)		
ROE average equity** = ($932 + $762) / 2		

What about PE?

I know PE is not supposed to be used to value a P/C insurance company. But it is a useful measure for most companies so let's see what it has to say.

If we use Yahoo Finance's current earnings estimate for Fairfax for FY 2023, we can see Fairfax is currently trading at a PE of 6x. That is crazy low. Both when compared to peers and the market in general.

Fairfax (US$)	**Feb 2, 2024**	
Share Price	$1,031	
2023 Earnings Estimate	$173	Yahoo Finance Est
P/E	6.0	

Summary

Fairfax is a high quality company delivering top-tier ROE. Trading at what looks to be crazy cheap valuation as measured by both P/BV and PE.

Is there anything that can explain this disconnect?

Yes. The narrative surrounding the company is in need of an update. The part driven by psychology.

Thanks for hanging in there. We've come full circle. Let's finish connecting the dots.

Part 4 - Narrative change and multiple expansion

> "Although expectations of the future are supposed to be the driving force in the capital markets, those expectations are almost totally dominated by memories of the past. Ideas, once accepted, die hard." *Peter Bernstein*

Fairfax and narrative

Fairfax had one analyst attend their Q3 conference call. Tom MacKinnon/BMO, you get a gold star from the teacher. The lack of interest in Fairfax in the analyst community suggests to me that the old narrative is still firmly in place.

After all, it is Fairfax. That shitty little Canadian insurance company. Right?

Even Rodney Dangerfield would be surprised at the lack of respect Fairfax still gets today - even though it is a top 20 global P/C insurer and now one of the top 30 Canadian companies in terms of market cap.

Yes, but the stock is a dog! Woof! Right? Fairfax has probably been one of the best performing large cap stocks in Canada over the past three years (the best?). But, hey, don't let the facts get in the way of a good narrative.

Fairfax	Share	YOY			YOY	
(US$)	Price	change		S&P500	change	
Dec 31, 2020	$341		increase	3,756		increase
Dec 31, 2021	$492	44%	over	4,766	27%	over
Dec 31, 2022	$594	21%	past 37	3,840	-19%	past 37
Dec 31, 2023	$921	55%	months	4,770	24%	months
Feb 2, 2024	$1,031	12%	202%	4,959	4%	32%

To be fair, the quality of the research on Fairfax has been getting better, especially over the last year. I recently read Jaeme Gloin/National Bank's Q4-2023 earnings preview for Fairfax and i had to wipe the tears from my eyes when i was done - it was that good. And not because he upped his price target to $C2,000. It was because of the facts and logic he provided readers - the detailed build - which he used to arrive at his conclusions (final earnings estimate, multiple and price target). It was clear Jaeme has actually put in the work to understand the Fairfax as it exists today (that doesn't mean he is ignoring the past).

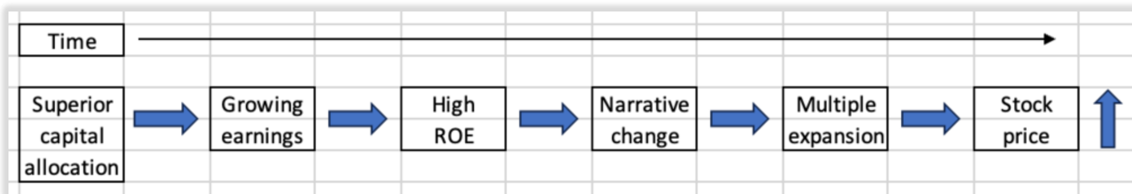
But there is also, IMHO, still one piece of simply terrible stuff out there. 'Crazy uncle' bad. This one is so steeped in the past it reads like it was actually written 10 years ago. (Maybe it was…. I better check the date.) Anyone who follows Fairfax closely knows the report that I am referencing. Now when you can go unnamed - and yet people know who you are? Well, that's pretty impressive. But is it really?

The good news is the old narrative around Fairfax will eventually be laid to rest. And that's because you can only ignore the facts and the fundamentals for so long.

Multiple expansion

My view is 2024 could well be the year when we get to an inflection point in the narrative for Fairfax. In fact, it looks like it might have started as we begin 2024. In January the P/BV multiple has expanded from 1.0 to 1.1.

As the narrative gets updated, Fairfax will shift from being valued as a poorly run company delivering poor results to being valued as a well-run company delivering very good results. In turn, this should result in multiple expansion. Yes, Fairfax will need to do its part - and continue to deliver solid results.



So, with Fairfax today, it looks like we have a situation where:

1. Earnings are growing
2. Multiple is expanding
3. Share count is falling

And all three happening at the same time? That is when the big money is made.

Part 5 - Multiple expansion - What does the math look like?

The example below is not intended to be a forecast. Rather it is intended to demonstrate to investors the power of multiple expansion (when it happens). Readers can overlay their own assumptions as they see fit.

To keep our analysis simple, we are going to use Dec 31, 2023 as our starting point. Let's be conservative and assume Fairfax only earns $150 in 2023 (instead of the forecast of $170). Let's also assume Fairfax continues to pay a $15 dividend. Let's be conservative and assume Fairfax grows earnings at 6% per year.

Now for the fun part. Let's assume the P/BV multiple expands from 1x at Dec 31, 2023 (where it was) to 1.3x at Dec 31, 2026. A multiple of 1.3x would get Fairfax to the lower band when compared to peers - I think it is a conservative number.

Given the inputs above, what is the return for investors over 3 years?

The total increase is 100%. A double over 3 years. Of the total increase, about 50% is driven by earnings. And 50% is driven by multiple expansion. Yes, multiple expansion is rocket-fuel to a stock.

Fairfax: Impsct of Multiple Expansion					3-Year
	2023	2024	2025	2026	Return
EPS *	$150	$158	$165	$174	
Growth	6.0%				
Dividend		$15	$15	$15	$45
BV at YE **	$932	$1,075	$1,225	$1,384	5%
Multiple at YE	1.0	1.2	1.25	1.3	
Stock Price at YE	$921	$1,289	$1,531	$1,799	
Increase / share		$369	$242	$267	$878
		40%	19%	17%	95%
Total					**$923**
					100%

EPS * to be conservative, let's lower 2023 EPS to $150.
BV at YE** using Yahoo Finance Q4 earnings estimate

Appendix - Is growth in book value a good measure of quality?

I wasn't able to find a good place to insert this into my post above. But I think it is important so I am including it here.

The growth in book value over time is another way to assess the quality of a P/C insurance company. In some ways, it might be the best way. Because it includes all the 'messy' stuff that might not be included in ROE (like unrealized losses in bonds).

How does Fairfax stack up when compared to peers like Markel, WR Berkley and Chubb?

Over the past 5 years Fairfax's has grown book value at a CAGR of 16.6%. None of the other 3 companies come close to that performance. It should be noted, Fairfax, WR Berkley and Chubb all pay a modest dividend. Markel does not.

Yes, change in book value is just another important measure that points to Fairfax being a very high quality P/C insurance company.

P/C Peer	Dec 31	Dec 31	Book Value Per Share		
Comparison	2023	2018	5 Year Change		Approx
	BV per Share		$	%	CAGR
Fairfax *	$932.35	$432.46	$499.89	116%	16.6%
Markel	$1,095.95	$653.85	$442.10	68%	10.9%
WR Berkley	$29.06	$19.81	$9.25	47%	8.0%
Chubb	$146.83	$109.56	$37.27	34%	6.0%

Note: Fairfax, WR Berkely and Chubb all pay dividends; Markel does not.
* Fairfax Dec 31, 2023 BV/share = $876.55 + $55.80 (Yahoo) = $932.35

What is the best way to value Fairfax today? As an insurance company or as a turnaround?

October 12, 2023

Fairfax has been an exceptionally difficult company for investors to value for the past three years. And especially right now (given the sharp rise in the stock price). Even investors who have followed the company closely for many years are having a hard time. New investors don't stand a chance.

Mr. Market is saying Fairfax has a fair value today of $832/share (that is where the stock closed October 12, 2023). I think the stock is still wicked cheap. Lots of other smart investors feel the stock is only mildly cheap.

<u>What is the fundamental problem?</u>

There is no consensus of what level of earnings the collection of assets that Fairfax currently owns can deliver on a regular basis moving forward. Or what to expect for the next 3 to 5 years.

Most investors prefer to use book value as their primary tool to value Fairfax. It is an insurance company after all. And using book value is supposed to be the proper way to value an insurance company. Using book value also conveniently allows an investor to largely ignore earnings (coming up with an estimate). And given the lack of consensus around earnings for Fairfax… well isn't that a good thing?

Well, easy and good are not the same thing.

<u>What is the best way to value Fairfax today?</u>

Just like any job, we need to pick the right tool. To do this we need to answer the following question.

<u>Is Fairfax an insurance company or a turnaround play?</u>

No, this is not a trick question. The answer, of course, is that Fairfax today is both. **But we are talking here about how to value Fairfax as a company.**

My view is today Fairfax should be valued primarily through the lens of a turnaround play. Not as an insurance company.

<u>Does it make that much of a difference?</u>

It makes a huge difference.

Using book value (P/BV and ROE) to value insurance companies with relatively consistent financial results over a 5 or 10 year period makes a lot of sense. But using book value (P/BV and past ROE) as the primary measure to value a turnaround like Fairfax makes little sense, especially when they are still in the middle of the earnings part of the turnaround.

The problem with book value (P/BV and ROE) is it is a 'rear view mirror' valuation measure - it does a great job of telling you what has happened. And for lots of insurance companies what 'has happened' is likely to continue to happen in the future. So, using book value (P/BV and ROE) as a primary valuation tool makes sense.

But for a turnaround like Fairfax, where a massive amount of change is happening - which is leading to much higher earnings - focussing primarily on the past is going to mess investors up. It is going to cause them to way under estimate future earnings. This in turn is going to cause them to under value the company. And that is going to lead to poor investment decisions.

A lot of investors who follow Fairfax are probably wondering how they missed the big move in the stock over the past 3 years. My guess is the key issue is too much 'rear view mirror' analysis and not enough 'looking out the front windshield' analysis. The difference between valuing a stodgy insurance company versus valuing a turnaround.

<u>How should an investor value a turnaround?</u>

Let's look to Peter Lynch for some insight. Peter Lynch loved turnarounds. It was one of the 6 buckets he used to classify his stock investments. Classifying stocks properly at the beginning of the process is critical. Because the classification determines the proper method to use to analyze the stock.

<u>To value a turnaround, it is critical to do three things:</u>

1. Understand what went wrong.
2. Confirm that whatever went wrong has indeed been fixed.
3. Focus in on evaluating the assets and estimating the trajectory of earnings.

<u>1.) What went wrong at Fairfax?</u>

Fairfax has three economic engines: insurance, investments - fixed income and investments - equities/derivatives.

Fairfax's insurance business has been a solid performer over the past decade. And their investments - fixed income economic engine has also performed well. The issue at Fairfax was the investments - equities/derivatives engine.

The good news for Fairfax was the solution to their poor performance was fully within their control. They just needed to stop doing some really dumb things (putting it politely) in one part of the company.

<u>2.) What was the fix?</u>

To right the ship in the equities/derivatives engine, Fairfax did a few things:

- End the equity hedge/shorting strategy. The equity hedge positions were exited in late 2016. The final short position was sold in late 2020. Done.
- Make better equity purchases. This started in 2018. Done.

- Fix poorly performing equity purchases from 2014-2017. This started in 2018 and looks like it was largely completed in 2022. Done.

But Fairfax didn't stop here. They did even more:

- Since 2020, they have made at least one brilliant decision each year:
    - Late 2020/early 2021: initiated the FFH total return swap position, giving exposure to 1.96 million Fairfax shares at $373 share (resulting in a $900 million pre-tax gain to date)
    - Late 2021: bought 2 million Fairfax shares at $500/share (book value is currently $834/share and intrinsic value is likely well over $1,000).
    - June 2022: sale of pet insurance for $1.4 billion ($992 million after-tax gain).

And the insurance gods have also been smiling on Fairfax:

- A hard market in P/C insurance started in Q4, 2019. It looks like it will continue into 2024.

And if all that wasn't enough, the macro gods also decided to smile on Fairfax, delivering to the company their biggest gift yet:

- After dropping interest rates to close to zero in late 2021, the Fed pivoted and spiked rates to more than 5% in 2023. Fairfax navigated their $38 billion fixed income portfolio through the treacherous storm perfectly - and the gold ($billions) is literally raining down today.

So, Fairfax not only stopped doing dumb things, they also started hitting the ball out of the park. At the same time both the insurance and macro gods started smiling on the company.

Each of these things on their own would have caused earnings to grow significantly over their historical trend. Stacked one on top of the other - well earnings have exploded higher.
In short, the turnaround at Fairfax that began back around 2018 now looks complete. But importantly, the lift to earnings will likely take a few more years to fully play out.

3.) What is happening to earnings at Fairfax

We are going to focus on operating income given this is considered the quality part of earnings for an insurance company. Operating income averaged $1 billion ($39/share) each year for 5 years from 2016-2020. From this base operating income has:

- Doubled to $1.8 billion in 2021.
- Tripled to $3.1 billion in 2022.
- Is on pace to quadruple to $4.3 billion in 2023.
- Is on pace to quintuple to $4.9 billion, or $214/share, in 2024.

How would an investor focussed primarily on book value have seen any of this coming? The answer is easy… they would have completely missed it. In fact, they probably still are missing it.

Fairfax - Operating Income									
October 12, 2023	**2016**	**2017**	**2018**	**2019**	**2020**	**2021**	**2022**	**2023E**	**2024E**
Underwriting profit - ins & reins.	$576	-$642	$319	$395	$309	$801	$1,105	$1,271	$1,294
Interest & dividends	$555	$559	$784	$880	$769	$641	$962	$1,945	$2,525
Share of profit of associates	$24	$201	$221	$170	-$113	$402	$1,015	$1,075	$1,050
Operating income - ins & reins	**$1,155**	**$118**	**$1,323**	**$1,444**	**$965**	**$1,844**	**$3,082**	**$4,291**	**$4,869**
Per share	$50	$4	$49	$54	$37	$77	$132	$186	$214
Shares Outstanding Dec 31	23.1	27.75	27.2	26.8	26.2	23.9	23.3	23.1	22.7
	2016	**2017**	**2018**	**2019**	**2020**	**2021**	**2022**	**2023E**	**2024E**
Earnings Per Share	-$24	$67	$12	$73	$7	$129	$47	$151	$158
Dividend	$10	$10	$10	$10	$10	$10	$10	$10	$10
Year End Book Value Per Share	$367	$450	$432	$486	$478	$631	$658	$903	$1,051
Return On Equity (average)	-7%	16.3%	2.7%	15.9%	1.4%	23.3%	7.2%	18.1%	16.1%
						IFRS-17	$762		

<u>What are we learning about Fairfax's collection of assets?</u>

Beginning as far back as 2021, investors were getting glimpses that something good was happening at Fairfax. In 2022, it was becoming obvious that 'new Fairfax' had arrived - but the good news was masked in the top line results by the bear market in financial markets and the large unrealized losses in fixed income and equities. But the change was obvious to those of us who followed the company closely. In 2023, the story continues to improve. And 2024 looks even better.

What we are learning is Fairfax was significantly under earning on its collection of assets for much of the past decade. But all the shackles that were holding earnings down have now been removed. Management is executing exceptionally well. For the first time in the company's history, the three economic engines are all delivering record results at the same time: insurance, investments - fixed income and investments - equities/derivatives.

Investors are just starting to get a look at what the true (normalized) earnings power of Fairfax is on a go forward basis. And the number is far higher than anyone dreamed possible.

<u>What is the valuation of Fairfax today?</u>

Board members probably wonder why I have been so focussed on earnings in my analysis of Fairfax the past two years. Well, now you know why. I view Fairfax currently as a turnaround type of investment - and a heavy focus on earnings and assets is the only rational way to analyze the company today.

It's not that I don't pay attention to book value. I do. I just have never trusted how useful it is a tool to help me better understand its earnings power of the company today.

My current estimate is Fairfax will earn about $150/share in 2023. I think that is a good baseline to use for earnings moving forward. If my analysis is right then that means Fairfax is trading at a PE of 5.5 x my estimated 2023 earnings. I think that is nuts.

Fairfax Financial (US$)	
Stock Price - Oct 12, 2023	$832
2023 Earnings Estimate	$150
P/E	5.5
Book Value - June 30, 2023	$834
P/BV	1.00
ROE	18%

What does the future hold?

> "Companies don't stay in the same category forever. Over my years of watching stocks, I've seen hundreds of them start out fitting one description and end up fitting another."
>
> *Peter Lynch - One Up On Wall Street*

Over the next couple of years, we will all come to better understand Fairfax. And what its collection of assets are capable of delivering. What the true 'normalized' earnings power of the company is. At that point in time, the turnaround will long be over. And Fairfax will revert to being another predictable, boring old insurance company. And at that time, the valuation metrics (like book value, P/BV and ROE) generally used for valuing boring old insurance companies will again be appropriate to use for Fairfax.

If Fairfax is able to deliver strong earnings growth in the coming years the much improved results will slowly get baked into its historical numbers. That is when more traditional insurance investors will start to 'discover' how well managed Fairfax is. And how cheap the stock is. As this process plays out the P/BV multiple will likely expand significantly from 1.0 today to something more in line with peers, perhaps north of 1.3 (perhaps higher).

_________-

Another reason Peter Lynch liked turnarounds:

> "The best thing about investing in successful turnarounds is that of all the categories of stocks, their ups and downs are least related to the general market." *Peter Lynch - One Up on Wall Street*

Fairfax is up 144% since December 31, 2020. The S&P500 is up 16%. Fairfax's outperformance over the S&P500 over the past 33 months has been an amazing 128%. Yes, Peter Lynch is one smart dude.

Fairfax	stock price (US$)	increase	increase over past 33 months	S&P500 (US$)	increase	increase over past 33 months
31-Dec-20	$340.94			3,756		
31-Dec-21	$492.13	44%		4,766	27%	
31-Dec-22	$594.12	21%		3,840	-19%	
12-Oct-23	$832.32	40%	144%	4,350	13%	16%

Peter Lynch on Turnarounds

“These are stocks that are battered down or they are hated companies, or they have been forgotten about. They are depressed in price but you have determined some one thing or a few things that have the potential for reversing this company’s fortunes independent of the industry getting better, or the economy getting better.

“You always have to do a balance sheet check on any company. This includes turnarounds. Do they have enough cash to make it through the next 12 months or the next 24 months? Do they have a lot of debt that’s due right now? These are important questions to answer.

“Make sure you understand and believe in the plan to restore corporate profits. It is all internal. They are doing something, either a new product, new management, cutting costs, getting rid of something. Something inside the company that allows them to improve themselves.

“Lots of turnarounds never happen, but a few winners can make up for a lot of losers. What’s important is to wait for the actual evidence of the turnaround occurring, not just the symptoms. (With) the turnaround, you have plenty of time. So just don’t buy on the hope. Wait for the reality. Turnarounds are so big it is worth waiting to get some real evidence.”

https://youtu.be/DYyLrrQ0Os4?si=5ax4xmZr0OiGxXUP

How Does Fairfax's Valuation Compare to Other P/C Insurers?

February 21, 2024

There are lots of methods an investor can use to value a company and its stock price. In this post, we are going to use a method called 'relative valuation.' We are going to try and see what we can learn about Fairfax's current valuation by comparing the company to a group of other P/C insurers.

We are going to keep the analysis very top line. In terms of time-frame, we are going to use the last 5 years. This is a good length of time to get a reading on the performance of the management teams for each company. And it also smooths out the impact of large short term events like catastrophes, Covid and the big swing in interest rates.

Who are we going to look at?

Below is the list of the seven P/C insurers we will compare (listed in alphabetical order):

- AIG: the fallen star; a turnaround play today.
- Berkshire Hathaway: historically, the gold standard; now more of a conglomerate than P/C insurer. We include it for fun.
- Chubb: big, traditional insurer; international in scope.
- Fairfax Financial: a turnaround play; about 30% of investments are in equities; international in scope.
- Intact Financial: largest P/C insurer in Canada; expanding globally.
- Markel: baby Berk; US focus
- WR Berkley: traditional insurer; US focus

To state the obvious: all P/C insurance companies have unique business models. Berkshire Hathaway has not released Q4, 2023 results so for them I have used an estimate for 2023YE book value and 2023 EPS.

The most important metric used by investors and analysts to value a P/C insurance company is book value. Yes, it has its flaws. However, it is a good place to start.

5-Year Change in Book Value

"In other words, the percentage change in book value in any given year is likely to be reasonably close to that year's change in intrinsic value." Warren Buffett

We are going to look at the change in book value for the 5-year period from Dec 31, 2018 to December 31, 2023. We have sorted the results in the table below from the best to the worst performers.

So which company has increased BVPS the most?

Fairfax Financial.

Fairfax has increased BV by 117% over the past 5 years, a CAGR of 16.8%.

Were you expecting that? I bet you weren't expecting that.

The second surprise is the size of the outperformance by Fairfax over all peers. For example, Fairfax's BV CAGR is 10% better than that achieved by Chubb - that is serious outperformance. Don't get me wrong, Chubb is a quality company.

In the quote above, Warren Buffett suggests investors should use the annual change in book value as a rough approximation of the change in intrinsic value for a company. Using Buffett's quote as a guide, I think we can safely say that Fairfax has increased intrinsic value over the past 5 years at a much faster pace than its P/C insurance peers.

P/C Insurance - 5-Year Change in Book Value Per Share
Dec 31, 2018 to Dec 31, 2023

	Book Value		5-Year		Annual Dividend	
US$	**2023 YE**	**2018 YE**	**Change**	**CAGR**	**$/Share**	**Yield**
Fairfax	$939.65	$432.46	117%	16.8%	$15.00	1.5%
Berkshire B*	$265.00	$141.67	87%	13.3%	n/a	n/a
Intact Fin (C$)	$81.71	$48.73	68%	10.9%	$4.84	1.9%
Markel	$1,095.95	$653.85	68%	10.9%	n/a	n/a
WR Berkley	$29.06	$19.81	47%	8.0%	$0.44	0.5%
Chubb	$146.83	$109.56	34%	6.0%	$3.44	1.4%
AIG	$65.14	$65.04	0%	0.0%	$1.44	2.1%

Berkshire B* 2023YE book value is an estimate.

Note: five of the seven companies pay a dividend (and WR Berkley has also paid special dividends).

Why has Fairfax's performance been so strong?

The management team at Fairfax has been executing exceptionally well over the past 5 years. Especially when it comes to capital allocation. I recently wrote a long post on this topic so I am not going to repeat it here.

How have shareholders been rewarded?

5.13-Year Change in Share Price

We are going to look at the change in the share price for the 5.13-year period from Dec 31, 2018 to February 16, 2024. Once again, we have sorted the results in the table below from the best to the worst performers.

Which company has seen their share price increase the most?

Three companies are bunched together as the top performers - WR Berkley, Fairfax Financial and Intact Financial. Including dividends, these three companies have delivered a CAGR of around 20% to investors over each of the past 5.13 years. That is outstanding.

Berkshire Hathaway, Chubb and AIG can be grouped in the next performance band. Including dividends, they have delivered a CAGR of about 14% which is quite good. And Markel has been the clear laggard with a CAGR of about 7%.

Another key takeaway is the performance of the group as a whole has been very good. Six of the seven companies listed have delivered a very good return to investors over the past 5.13 years. For reference, over the same 5.13 years, the S&P500 increased 100%, which was a CAGR of 14.4% (not including dividends).

P/C Insurance - 5.1-Year Change in Share Price
Dec 31, 2018 to Feb 16, 2024

	Share Price		Change		Annual Dividend	
	Feb 16 '24	2018 YE	Total	CAGR	$/Share	Yield
WR Berkley	$82.61	$32.85	151%	19.7%	$0.44	0.5%
Fairfax	$1,022.00	$440.08	132%	17.8%	$15.00	1.5%
Intact Fin (C$)	$228.67	$99.19	131%	17.7%	$4.40	1.9%
Berkshire B	$405.99	$204.18	99%	14.3%	n/a	n/a
Chubb	$250.90	$129.18	94%	13.8%	$3.44	1.4%
AIG	$70.04	$39.41	78%	11.9%	$1.44	2.1%
Markel	$1,461.50	$1,038.05	41%	6.9%	n/a	n/a

Now let's put book value and share price together and see what we can learn about valuation.

Current Price to Book Value (P/BV)

At 2.8, Both Intact and WR Berkley trade at the highest P/BV multiple. This is not surprising given they also saw the biggest increases in share price over the past 5 years.

Does anything in the chart below jump out?

Yes. Fairfax looks out of place.

Fairfax has been compounding book value at the highest rate over the past 5 years. So how can it also be trading at the lowest P/BV (i.e. the cheapest) valuation? That makes no sense.

P/C Insurance Comparison			Share	Book
Feb 16, 2024			Price	Value
	P/BV		Feb 16 '24	2023 YE
WR Berkley	2.84		$82.61	$29.06
Intact Fin (C$)	2.80		$228.67	$81.71
Chubb	1.71		$250.90	$146.83
Berkshire B	1.53		$405.99	$265.00
Markel	1.33		$1,461.50	$1,095.95
Fairfax	1.09		$1,022.00	$939.65
AIG	1.08		$70.04	$65.14

Let's look at another valuation measure and see what it tells us.

Price to Earnings Ratio (PE)

To keep things simple, I used reported EPS from 2023 for each of our seven companies. For Berkshire, who has not yet reported, I took the estimate from Yahoo Finance. For Intact Financial, who reported restructuring charges in Q4, I was generous and used the 2023 number in Yahoo Finance (which looks like it nets out the restructuring charges).

Does anything in the chart below jump out?

Yes. Fairfax looks out of place (again).

Fairfax has been compounding book value at the highest rate over the past 5 years. So how can it also be trading at the lowest PE (i.e. the cheapest) valuation? That makes no sense.

P/C Insurance - 2023 Net Earnings and Trailing PE				
			Share	Net
	Trailing		Price	Earnings
	P/E		Feb 16 '24	2023
Berkshire B*	25.2		$405.99	$16.14
Intact Fin * (C$)	19.5		$228.67	$11.70
WR Berkley	16.4		$82.61	$5.05
AIG	14.1		$70.04	$4.98
Chubb	11.5		$250.09	$21.80
Markel	9.9		$1,461.50	$146.98
Fairfax	5.9		$1,022.00	$173.24
Berkshire B* and Intact * - Net Earnings from Yahoo				

So, what can explain the disconnect between Fairfax's past performance (top-tier) and its valuation (bottom tier)?

To be fair, as we learned earlier in this post, Fairfax's stock price has been one of the top performers over the past 5 years. So investors clearly have been warming to the company. However, even with the strong performance in recent years, the stock's valuation continues to be at the bottom when compared to peers. Why is that?

Lack of understanding of the company.

Fairfax is still not a well understood company. Few investors (or analysts) have followed it in recent years. Yes, this is changing. But it will take time for people to get back up to speed with the company.

Fairfax is also a turnaround. And turnarounds are exceedingly hard to value - especially at the point when their business results hockey stick and turn higher.

The interesting thing with Fairfax though is the turnaround was actually completed back in 2021. But because the company was not followed back then pretty much no one noticed (well, except for a bunch of investors on the investing forum 'Corner of Berkshire and Fairfax').

Operating earnings and the future.

Over the past 5 years, Fairfax has quietly completed one of the of great turnarounds in recent Canadian business history. Operating earnings at Fairfax have exploded - and that is not hyperbole.

Operating earnings averaged $1 billion ($39/share) at Fairfax for the 5-years from 2016 to 2020. In 2023, operating earnings were $4.4 billion ($193/share). Per share, operating earnings have increased 395% over their baseline from just a couple of years ago.

Importantly, this new level of operating earnings, around $200/share, is sustainable. This was discussed on Fairfax's Q4 conference call. Operating earnings are considered the highest quality type of earnings a P/C insurance company can deliver. Think about what this new development means for Fairfax's future results - earnings, ROE, book value and multiple.

Fairfax - Operating Income									
February 16, 2024	**2016**	**2017**	**2018**	**2019**	**2020**	**2021**	**2022**	**2023**	**2024E**
Underwriting profit - ins & reins.	$576	-$642	$319	$395	$309	$801	$1,105	$1,522	$1,270
Interest & dividends	$555	$559	$784	$880	$769	$641	$962	$1,896	$2,250
Share of profit of associates	$24	$201	$221	$170	-$113	$402	$1,015	$1,022	$1,100
Operating income - ins & reins	**$1,155**	**$118**	**$1,323**	**$1,444**	**$965**	**$1,844**	**$3,082**	**$4,441**	**$4,620**
Per share	$50	$4	$49	$54	$37	$77	$132	$193	$204
Shares Outstanding Dec 31	23.1	27.75	27.2	26.8	26.2	23.9	23.3	23	22.7
Operating Income ROE	13%	1%	11%	12%	8%	14%	21%	23%	20%
E = average equity	5-Year Average (2016-2020) = 8.9%					3-Yr Avg (2021-2023E) = 19.5%			

What did we learn in the post?

Warren Buffett tells us that the change in book value per share is a good approximation for change in intrinsic value. Over the past 5 years, Fairfax has delivered a cumulative increase in BVPS of 117%, which is a CAGR of 17.8%. Simply outstanding. This is best-in-class performance compared to peers.

We also learned that operating earnings have spiked at Fairfax by close to 400% over the past 3 years from $39/share to about $200/share today - and that the higher amount is durable. This suggests Fairfax should be able to continue to deliver top-tier performance when compared to peers in the coming years.

We also learned that Fairfax currently has the cheapest valuation - its P/BV is 1.09 and its PE is 5.9. Fairfax's valuation is significantly below peers.

So an investor today is able to buy the top performing P/C insurance company - with among the best future prospects - at the cheapest valuation. In short, the risk/reward set-up for Fairfax has rarely looked better. I think that guy in Omaha would call Fairfax a very fat pitch.

"The way of the successful investor is normally to do nothing -- not until you see money lying there, somewhere over in the corner, and all that is left for you to do is go over and pick it up." Jim Rogers

P/C Insurance Companies - Comparison of Key Met

	5-Year CAGR BVPS	5.1-Year CAGR Share Price	P/BV	Trailing P/E	Current Dividend Yield
Fairfax	16.8%	17.8%	1.09	5.9	1.5%
Berkshire B	13.3%	14.3%	1.59	25.2	n/a
Intact Fin ($)	10.9%	17.7%	2.80	19.5	1.9%
Markel	10.9%	6.9%	1.33	9.9	n/a
WR Berkley	8.0%	19.7%	2.84	16.4	0.5%
Chubb	6.0%	13.8%	1.71	11.5	1.4%
AIG	0.0%	11.9%	1.08	14.1	2.1%

CAGR BVPS: Dec 31, 2018 to Dec 31, 2023
CAGR Share Price: Dec 31, 2018 to Feb 16, 2024
P/BV: Share price at Feb 16, 2023 and BV at Dec 31, 2023

The Evolution of Fairfax – The Multiple Streams of High Quality Income Phase

October 11, 2023

In prior posts, we have discussed operating earnings. In this post let's look at all of Fairfax's sources of income. What are they? What is their quality? How are they changing?

Why does sources of income matter?

'Quality earnings': of all the sources of income, operating income are generally considered to be the highest quality for P/C insurance companies because the sources are considered to be predictable and durable. Companies that generate the majority of their total earnings from operating income are considered to be higher quality. As a result, the stock prices of these companies usually trade at a premium valuation to peers.

Understanding sources of income and their trend should provide us with another important piece of information to help us understand Fairfax's valuation, especially when compared to peers.

Fairfax has 5 streams of income:

1. Underwriting profit
2. Interest and dividend income
3. Share of profit of associates (primarily Eurobank, Atlas, Exco, Stelco and GIG)
4. Non-insurance subsidiaries (primarily Recipe, Fairfax India, Thomas Cook, AGT, Grivalia Hospitality and Dexterra)
5. Net gains/losses on investments (mark to market equities, derivatives, fixed income, asset sales, including insurance)

The first three streams when added together give us all the important operating income.

Let's look at the average of these income streams over a 6-year period from 2016-2021:

Size: From 2016-2021, Fairfax generated in total an average of about $2.5 billion per year from the 5 income streams listed above. The total amount was quite volatile year-to-year.

Composition (split) of the average from 2016-2021:

- Net gains on investment was, by far, the largest income stream at 49% of the total.
- Interest and dividend income was the second largest bucket at 28%.
- Underwriting profit was the third largest largest at 12%.
- Share of profit of associates was 6%.
- Non-insurance subsidiaries was 4%.
- Operating income was 46%, or less than half of the total.

	Fairfax - Income Streams	2016-21 Avg													
	Updated: October 11, 2023	total	split	2016	split	2017	split	2018	split	2019	split	2020	split	2021	split
1.)	Underwriting profit - ins & reins.	$293	12%	$576	23%	-$642	-40%	$319	11%	$395	14%	$309	15%	$801	26%
2.)	Interest & dividends	$698	28%	$555	22%	$559	35%	$784	28%	$880	32%	$769	38%	$641	20%
3.)	Share of profit of associates	$151	6%	$24	1%	$201	13%	$221	8%	$170	6%	-$113	-6%	$402	13%
	Operating income - ins & reins	**$1,142**	**46%**	**$1,155**	**47%**	**$118**	**7%**	**$1,323**	**47%**	**$1,444**	**52%**	**$965**	**47%**	**$1,844**	**59%**
4.)	Non-insurance subsidiaries	$111	4%	$103	4%	$262	16%	$264	9%	$104	4%	-$139	-7%	$71	2%
5.)	Net gains/losses on investments	$1,213	49%	$1,213	49%	$1,213	76%	$1,213	43%	$1,213	44%	$1,213	59%	$1,213	39%
	Total Income Streams	**$2,465**	**100%**	**$2,472**	**100%**	**$1,593**	**100%**	**$2,800**	**100%**	**$2,761**	**100%**	**$2,039**	**100%**	**$3,128**	**100%**

<u>These splits fit the narrative of the company at the time (2016-2021)</u>:

The vast majority of income at Fairfax was being generated by 'gains on investments,' and these gains had massive swings each year (up and down) so Fairfax's reported results were quite volatile year to year (see chart below). Lots of volatility year to year = low quality earnings.

From 2016-2021, Fairfax earned an average of $44/share each year. Book value averaged $474/share. Its stock traded around $500/share during this time. Fairfax was valued at around 1.05 x BV and a PE of around 11.4. These multiples were well below peers.

<u>Important: net gains/losses on investments</u> - in the chart above an average number was used for each year from 2016-2021. Large negative numbers mess up the 'split' calculations. Importantly for our analysis, using an average number allows us to get a 6 year average that is a good representation of the split of the various income streams. The chart below shows the actual numbers for each year.

Actuals and Calculation of Average for 2016-2021	**Total 2016-21**	**Average Per Year**	**Actual Amounts For Each Year**					
			2016	**2017**	**2017**	**2019**	**2020**	**2021**
Net gains/losses on investments	$7,279	$1,213	-$1,204	$2,458	$194	$1,692	$430	$3,709
Includes 'Gain on sale/deconsol of ins sub' and 'Loss on repurchase of LT debt'								

<u>Let's look at the income streams for 2022</u>:

- We are going to look at 2022 on its own. 2022 was an anomalous year for global financial markets - we had the largest bear market in history in fixed income and, at the same time, a bear market in stocks. As a result, Fairfax had a $1.7 billion loss on investments in 2022. This was largely offset by a $1.2 billion gain from the sale of its pet insurance business (pre-tax). So, the final loss on investments came in at only $514 million.
- Operating income spiked higher to $3.1 billion. This number on its own was now larger than the average of the total of all income sources from 2016-2021.

In 2022, the impact of rising interest rates has been fully reflected in Fairfax's income statement and balance sheet. As a result, the fixed income portfolio/balance sheet has been largely de-risked from the impact of spiking interest rates.

At the same time, a significant shift in the composition of Fairfax's income streams that started in 2021 accelerated in 2022 - each of the 3 components of operating income increased to record levels.

Despite bear markets in both bond and stock markets, Fairfax was still able to generate a total of $2.6 billion from its 5 income streams in 2022.

	Fairfax - Income Streams (2022)		
	Updated: October 11, 2023	**2022**	**split**
1.)	Underwriting profit - ins & reins.	$1,105	42%
2.)	Interest & dividends	$962	37%
3.)	Share of profit of associates	$1,015	39%
	Operating income - ins & reins	**$3,082**	**117%**
4.)	Non-insurance subsidiaries	$61	2%
5.)	Net gains/losses on investments	-$514	-20%
	Total Income Streams	**$2,629**	**100%**

Let's look at my estimates for the earnings streams for 2023-2025:

This is where things get really interesting. Especially when compared to 2016-2021.

Size: From 2023-2025, my estimate has Fairfax generating an average of $5.8 billion per year from the 5 income streams. This is an increase of 132% over the run rate of $2.5 billion from 2016-2021.

Composition (split) 2023-2025 compared to composition from 2016-2021:

- Interest income is now the largest single item at 40% up from 28%.
- Underwriting profit is up nicely to 22% from 12%.
- The big mover, though, is share of profit of associates which increased to 19% from 6%.
- Operating earnings are now 80% of the total. That big increase from 46% from 2016-2021.
- Gains on investments are still a solid 17%. My estimate here is likely low - this is one reason why I think my total earnings estimate for 2023-2025 is mildly conservative.
- Non-insurance subsidiaries could grow significantly in the coming years. I think income of $300 million/year from this collection of companies is attainable looking out a couple of years. Were this to occur, Fairfax would have a meaningful 5th income stream

	Fairfax - Income Streams	**2023-25 Avg**		**2023**		**2024**		**2025**	
	Updated: October 11, 2023	**total**	**split**	**FY est**	**split**	**FY est**	**split**	**FY est**	**split**
1.)	Underwriting profit - ins & reins.	$1,259	22%	$1,271	23%	$1,294	22%	$1,211	20%
2.)	Interest & dividends	$2,284	40%	$1,945	36%	$2,525	43%	$2,381	40%
3.)	Share of profit of associates	$1,092	19%	$1,075	20%	$1,050	18%	$1,150	19%
	Operating income - ins & reins	**$4,634**	**80%**	**$4,291**	**79%**	**$4,869**	**82%**	**$4,742**	**80%**
4.)	Non-insurance subsidiaries	$133	2%	$50	1%	$150	3%	$200	3%
5.)	Net gains/losses on investments	$1,000	17%	$1,099	20%	$900	15%	$1,000	17%
	Total Income Streams	**$5,767**	**100%**	**$5,440**	**100%**	**$5,919**	**100%**	**$5,942**	**100%**

Conclusion:

Two stories are playing out simultaneously at Fairfax right now:

- a total earnings story - earnings are spiking.
- a quality of earnings story - the quality of earnings has improved dramatically in recent years

Importantly, the increases in both the size and quality of earnings looks sustainable.

Having multiple sources of income does a couple of things for the company:

- provides important diversification across both insurance and investments.
- makes the whole company more resilient to both insurance and economic cycles.
- generates much more consistent cash flows over time allowing the company to be highly opportunistic with capital allocation.

This should make Fairfax a more valuable company. It should trade today at a valuation multiple more in line with peers (if not a premium to some).

	Fairfax - Income Streams	**2016-21 Avg**				**2023-25 Avg**	
	Updated: October 11, 2023	total	split	**2022**	**split**	**total**	**split**
1.)	Underwriting profit - ins & reins.	$293	12%	$1,105	42%	$1,259	22%
2.)	Interest & dividends	$698	28%	$962	37%	$2,284	40%
3.)	Share of profit of associates	$151	6%	$1,015	39%	$1,092	19%
	Operating income - ins & reins	**$1,142**	**46%**	**$3,082**	**117%**	**$4,634**	**77%**
4.)	Non-insurance subsidiaries	$111	4%	$61	2%	$133	2%
5.)	Net gains/losses on investments	$1,213	49%	-$514	-20%	$1,000	17%
	Total Income Streams	**$2,465**	**100%**	**$2,629**	**100%**	**$5,767**	**100%**

What is reflected in Fairfax's valuation?

Investors have been warming to the Fairfax story. Fairfax's stock current trades at about $830 (Oct 11, 2023). Its stock price has increased 144% over the past 33 months (since Dec 31, 2020). However, Fairfax currently trades at a 5.5 x multiple to my 2023 estimated earnings (about $150/share). It is also trading at about 1 x book value ($834/share). These are very low multiples and much below peers.

This suggests to me that:

- Mr. Market is starting to understand the spiking earnings story at Fairfax.
- Mr. Market does not yet understand the much improved quality/durability of earnings story at Fairfax.

And that is because multiple expansion has not yet happened at Fairfax. Mr. Market does get things right over the medium term. My guess is as investors come to more fully understand 'new Fairfax' we will get multiple expansion in the coming years and Fairfax will trade at a multiple closer to peers. If this happens it would (along with continued growth in earnings and share buybacks) help power the stock price to much higher levels.

<u>The hard market in insurance</u>

There is a lot of hand wringing among investors today about the status of the hard market in insurance. When will it end? What will it mean for insurers? Do we get a sideways insurance market (not too hot or too cold)? Or do we a rapid descent into insurance hell - and a full-on soft market.

Underwriting profit makes up about 50% of total income for most insurers (with investments making up the other half - mostly from fixed income). So, what happens to insurance pricing in the future will impact the financial results of most insurance companies in a significant way.

For Fairfax, as we have just learned above, underwriting profit only makes up about 20% of total income from expected sources. As a result, where insurance pricing goes in the future will impact Fairfax far less than its insurance peers.

Fairfax's total earnings are now of a size, diversity and quality that maintaining strong underwriting profitability (perhaps mid-90's CR) can be even more of the focus moving forward at the insurance operations. Unlike other insurance companies, Fairfax's future will not be tied primarily to the insurance cycle. Its future will be tied to how well it does capital allocation. Capital allocation is increasingly becoming Fairfax's competitive advantage.

How to make the big money? Patience.

January 27, 2023

To state the obvious, outperforming the market averages is very difficult. Especially over a longer timeframe like 10 or 20 years. So why manage your own investments? Investors usually do it for the opportunity to make the big money - to materially outperform the market averages.

How can an investor do that? That is what we are going to explore in this post.

The post has been broken into the following sections:

1. Learning from the master: how did Buffett do it?
2. Time, compounding and exponential growth
3. What do investors actually do?
4. How to make the big money
5. Berkshire Hathaway
6. Fairfax Financial

> "In 58 years of Berkshire management, most of my capital-allocation decisions have been no better than so-so…
>
> "Our satisfactory results have been the product of about a dozen truly good decisions – that would be about one every five years.
>
> "The lesson for investors: The weeds wither away in significance as the flowers bloom. Over time, it takes just a few winners to work wonders. And, yes, it helps to start early and live into your 90s as well." *Warren Buffett - Berkshire Hathaway 2022AR*

Part 1: Learning from the master: How did Buffett do it?

Warren Buffett has been able to significantly outperform the market averages since 1965. Over the past 58 years (to YE 2022), Berkshire Hathaway stock has had a CAGR of 19.8%, which is about 2 times the CAGR of the S&P 500 of 9.9% (including dividends). Yes, Buffett has earned 'big money' for Berkshire Hathaway shareholders.

Berkshire Hathaway	
Compounded Annual Change - 1965-2022	
in Per-Share Market Value of Berkshire	19.8%
in S&P 500 with Dividends Included	9.9%

But here is what is really interesting. Buffett readily admits most of his capital allocation decisions over this 58-year time period were 'so-so.'

He goes on to explain that his significant outperformance was driven by a small number of 'truly good decisions'. Buffett puts the number at 12, or one about every 5 years.

This looks like it could be important. Let's explore this further.

<u>What is Warren Buffett's greatest attribute?</u>

Yes, this is kind of a dumb thing to ask. Let's do it anyway. What is it about Warren Buffett that has allowed him to consistently generate such outstanding results over the past 58 years?

- Intellect?
- Work ethic?
- Thirst for knowledge?
- Temperament?
- Character?
- Self-awareness?
- Management skills?

Obviously, all of the above attributes are important and will help investors achieve success. But lots of investors have many of these attributes - and yet they still underperform the market averages over time (let alone outperform to the degree that Buffett did).

<u>Is there something else, not listed above, that perhaps explains Buffett's significant outperformance?</u>

I think there is something else…

I think Buffett's greatest strength might be his patience.

Before you throw your phone/tablet in disgust, let me explain. We need to peel the layers back.

Buffett's holding period is not months. Or years. For his 'truly good decisions,' the investments that become needle movers for Berkshire Hathaway, his holding period can be measured in decades. And that is very different from almost any other investor out there. That is something Buffett does than pretty much no one else does. (Please name another successful investor who did it this way… i can't think of another one.)

After patience, I think Buffett's next greatest strength might be how he sizes his positions, especially his best ideas. And not just at the time of purchase - but also over time. How to size a position is exceptionally difficult to do and is a topic that deserves its own post - so we will not explore it further here.

There are a couple of lessons here:

- Really, really good investment opportunities are exceptionally rare. Over his lifetime, Buffett points to 12 that worked out for him - or one about every 5 years.
- But finding a great investment is not enough on its own. Great patience is also required. It can take a decade or more for some investments to fully bloom.

Of the two skills (finding a great investment and having great patience with it) the second is the one that is incredibly rare today.

Part 2: Time, compounding and exponential growth

What is the greatest advantage of an investor? It is time.

Why time? Time is what allows compounding to work its magic.

Compounding is simple to explain but wicked difficult for most people to actually understand. I like the description below. It is 'boring' for years and then very 'exciting'.

Given enough time, compounding inevitably results in exponential growth. Or at least the is what one would think. More on this later.

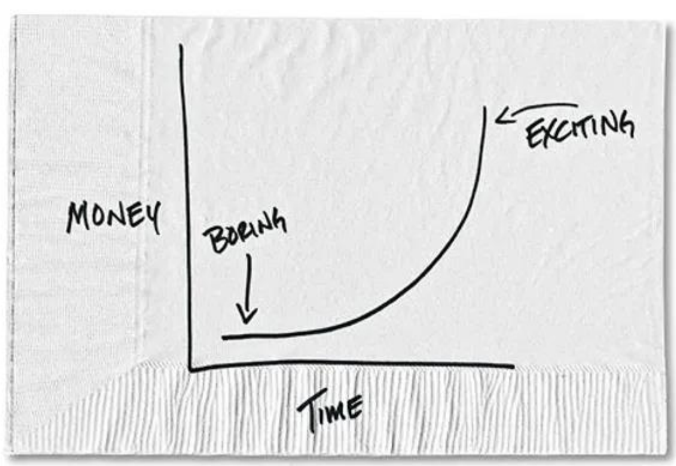
The goal of all investors is to get their portfolio to the 'exciting' part of compounding curve (the hockey stick part) - because it is life changing when it happens.

Buffett's genius?

It is understanding that patience and time are two sides of the same coin. Together, they allow an investor to fully maximize the benefits of compounding. This in turn, can lead to exponential growth.

Patience: this is how the big money is made.

Compound Interest (drawing by Carl Richards)



Let’s take a quick trip into the archives

One of my favourite all time books on investing is Reminiscences of a Stock Operator. It was first published all the way back in 1923 (in serial form over two years in The Saturday Evening Post).

Of all the memorable quotes in this book the following might be my favourite:

> “And right here let me say one thing: After spending many years in Wall Street and after making and losing millions of dollars I want to tell you this: It never was my thinking that made the big money for me. It always was my sitting. Got that? My sitting tight! It is no trick at all to be right on the market. You always find lots of early bulls in bull markets and early bears in bear markets. I've known many men who were right at exactly the right time, and began buying or selling stocks when prices were at the very level which should show the greatest profit. And their experience invariably matched mine - that is, they made no real money out of it. Men who can both be right and sit tight are uncommon. I found it one of the hardest things to learn. But it is only after a stock operator has firmly grasped this that he can make big money…” ***Reminiscences of a Stock Operator***

The lesson: Finding a great investment is hard. Holding the investment for years, perhaps decades - that is much more difficult. Should we be surprised that Buffett is in a league of his own?

Part 3: What do investors actually do?

> “Selling your winners and holding your losers is like cutting the flowers and watering the weeds.”
> *Peter Lynch*

Warren Buffett liked this quote so much he contacted Peter Lynch and asked him if he could use it.

What is the average holding period for retail investors?

I think it is around 5.5 months. And falling over time.

Retail investors are like Edward Scissorhands. The flowers in their garden don’t stand a chance.

Actually, we probably need to update Peter Lynch’s quote: these days, retail investors are so active buying and selling stocks in their portfolio - it’s like they completely raze their garden at least one time every year or two. What’s the chance the flowers are getting cut? Probably 100%. Should we be surprised that most retail investors achieve such poor results over time?

What about the professional/smart money?

The performance of professional/smart money is measured by investors quarterly… so they can't be patient with their holdings. Sub-par results over a couple of quarters and retail investors start to pull the plug. The professional/smart money has to chase short-term performance if they want to stay in business (or get paid their bonus) - which usually means owning whatever are the most popular stocks at a given time (the list of which is always changing).

The bottom line, 'patience' is not a word that is part of retail and professional investors vocabulary or in their toolbox.

Patience is primarily the stomach part of investing. Not the brain part. This probably tells us something…

Ben Carlson has a good article on the subject of holding period

Buy & Hold is Dead, Long Live Buy & Hold (Feb 2023)
- https://awealthofcommonsense.com/2023/02/buy-hold-is-dead-long-live-buy-hold/

(As an aside, 'The Compound' has become one of my favourite podcasts to listen to. Ben, Josh, Michael and guests are great. They have a bunch of different formats depending on what you are interested in.)

Taking profits

Why do retail investors turn their portfolio over so much? Lot's of reasons. To buy something they think is better. To get rid of a mistake. To try and time the market. Macro call. Hot tip. I could list another +20 'good' reasons.

Let's be optimistic. We are told taking profits is a sensible thing to do. Yes?

But remember, in this post, we are trying to learn how to make the big money.

Here is another great quote from the book 'Reminiscences of a Stock Operator':

> "They say you never grow poor taking profits. No. you don't. But neither do you grow rich taking a four-point profit in a bull market." *Reminiscences of a Stock Operator*

When investors sell their best ideas, they are cutting the flowers in their portfolio. And because the really good ideas (that actually work out) are exceptionally rare (Buffett found one about every 5 years), the proceeds are recycled back into inferior ideas - investors water their weeds. Of course, at the time investors don't think they are doing this (they think they are doing the opposite).

This is like throwing sand in the gears of the compounding machine we discussed earlier. And hurts investment results. Investors get stuck in the 'boring' stage (from the napkin drawing above). As a result, many investors in their lifetime never actually get to the 'exciting' stage - the hockey stick part of compounding that becomes life changing.

What does the investment industry have to say on this topic? I find it is helpful to follow the money. Incentives matter. A lot. How does everyone in the industry get paid? Fees. And fees generally come from activity. Action. Churn. Chasing short term performance. The exact opposite of patience.

Part 4: How to make the big money

Buffett's very simple model:

- Step 1: Identify a 'truly good' investment and size the position appropriately.
- Step 2: Exercise great patience and let it grow undisturbed for decades.

Truly great investments (the needle movers) are exceedingly rare. When you discover one, you need to size it appropriately. And then you hang on to it. For a long, long time.

Do we have any real-life examples of 'patience' actually working out for a retail investor?

Yes. A company named Berkshire Hathaway.

Part 5: Berkshire Hathaway

Investors have known for decades that Berkshire Hathaway was run by one of the best capital allocators of all time. All an investor had to do was buy shares and watch the Buffett flower bloom every year… bigger, brighter and more beautiful.

Importantly, investors had years to watch (learn) and get their position sized right.

How many investors followed Berkshire Hathaway over the decades? Lots.

How many investors never bought shares? Lots.

How many investors bought shares and then sold them after a small gain? Lots.

How many investors bought shares and then held them for a decade or longer? Very few. But the few who did so were able to build great wealth over time. These investors exercised great patience - and were richly rewarded.

These investors had a 'truly great idea' - buy Berkshire Hathaway stock. But their real genius - what separated them (and their returns) from all other investors - was their patience. Like Buffett, they held the stock for the long-term.

Why didn't these investors sell out? That is a great question. I don't know. Because I sold my Berkshire Hathaway every time I ever owned it (after what I thought was a nice gain). With hindsight, I was a dummy. I was happy making a small profit. And I completely missed the big move - when it was staring me right in the face.

So, what does all of this have to do with Fairfax? Maybe nothing. Maybe everything.

Part 6: Fairfax Financial

Similar to Berkshire Hathaway, Fairfax has an outstanding long-term track record. Fairfax has significantly outperformed the S&P 500 over the past 38 years (since the company was founded in 1985).

Fairfax Financial - 1985 to 2023	**Year End Value**		
Compounded Annual Change	**1985**	**2023**	**CAGR**
Fairfax - share price	$3.25	$1,223	16.9%
S&P 500	211	4,770	8.6%
*** dividends not included for both Fairfax and S&P 500**			

However, unlike Berkshire Hathaway, Fairfax had a pretty big stumble from about 2010-2017. The investing side of the business messed up (the insurance side of the business continued to perform well). Business results suffered. However, from about 2016 to 2020 the company got to work correcting its past mistakes. By 2021, the turnaround was largely complete.

Operating income has increased from a run rate of $1 billion/year from 2016-2020, to $1.8 billion in 2021, to $3.1 billion in 2022, to an estimated $4.4 billion in 2023. And it is poised to increase again in 2024 (my current estimate is $4.6 billion).

Since around 2018, Fairfax's capital allocation decisions have been very good - best-in-class among P/C insurers. I have written about this extensively in other posts so i am not going to rehash things here.

Bottom line, the set-up at Fairfax today - with both insurance and investment businesses - has never looked better.

Now I generally hate comparing Fairfax with Berkshire Hathaway because they are such different companies. But I am going to break my rule in this post.

Here is what I am wondering…

<u>Does Fairfax today look like a much younger Berkshire Hathaway?</u>

Here are some of the similarities I see between Fairfax today and a Berkshire Hathaway from 30 years ago:

1. Business model: Built squarely on the P/C insurance / float model (Berkshire Hathaway has more of a conglomerate business model today)
2. Capital allocation: Master capital allocator (Fairfax has been hitting the ball out of the park in this regard since 2018 - that is a pretty good timeframe to use to evaluate the current management team)
3. Significant, sustainable earnings: Current estimates have Fairfax earning a record of more than $4 billion in 2023. And the future outlook is promising.
4. Size: Fairfax is still small in size - good capital allocation decisions move the needle in terms of financial results (earnings and book value growth)
5. All of the above + the power of compounding = opportunity for exponential growth over the next decade. 'Time is the friend of the wonderful business' to quote Warren Buffett.
6. Valuation: Fairfax's stock is trading today at a very low valuation - both compared to P/C insurance peers and the overall stock market.

The set up today for Fairfax looks - to me - an awful lot like a much younger Berkshire Hathaway. Fairfax is poised to become a compounding machine in the coming years. If that happens, Fairfax would become what Buffett would call a 'truly good decision' for investors.

<u>Is Fairfax, once again, a buy and hold type of stock?</u>

I am warming to this idea. I think 5 years is a good amount of time to evaluate a management team - and the team at Fairfax has done an exceptional job over the past 5 years. This topic is important - let's give it the attention it deserves in a future post.

<u>Full quote by Warren Buffett from Berkshire Hathaway 2022AR</u>

"At this point, a report card from me is appropriate: In 58 years of Berkshire management, most of my capital-allocation decisions have been no better than so-so. In some cases, also, bad moves by me have been rescued by very large doses of luck. (Remember our escapes from near-disasters at USAir and Salomon? I certainly do.)

"Our satisfactory results have been the product of about a dozen truly good decisions – that would be about one every five years – *and* a sometimes-forgotten advantage that favors long-term investors such as Berkshire. Let's take a peek behind the curtain.

The Secret Sauce

"In August 1994 – yes, 1994 – Berkshire *completed* its seven-year purchase of the 400 million shares of Coca-Cola we now own. The total cost was $1.3 billion – then a very meaningful sum at Berkshire.

"The cash dividend we received from Coke in 1994 was $75 million. By 2022, the dividend had increased to *$704* million. Growth occurred every year, just as certain as birthdays. All Charlie and I were required to do was cash Coke's quarterly dividend checks. We expect that those checks are highly likely to grow.

"American Express is much the same story. Berkshire's purchases of Amex were essentially completed in 1995 and, coincidentally, also cost $1.3 billion. Annual dividends received from this investment have grown from $41 million to *$302* million. Those checks, too, seem highly likely to increase.

"These dividend gains, though pleasing, are *far* from spectacular. But they bring with them important gains in stock prices. At yearend, our Coke investment was valued at $25 billion while Amex was recorded at $22 billion. Each holding now accounts for roughly 5% of Berkshire's net worth, akin to its weighting long ago.

"Assume, for a moment, I had made a similarly-sized investment mistake in the 1990s, one that flat-lined and simply retained its $1.3 billion value in 2022. (An example would be a high-grade 30-year bond.) That disappointing investment would now represent an insignificant 0.3% of Berkshire's net worth and would be delivering to us an unchanged $80 million or so of annual income.

"The lesson for investors: The weeds wither away in significance as the flowers bloom. Over time, it takes just a few winners to work wonders. And, yes, it helps to start early and live into your 90s as well."

Is it time to sell Fairfax?

October 12, 2023

Fairfax's stock has delivered a cumulative 144% return to investors over the past 33 months (since Dec 31, 2020). It has also paid three $10 dividends each year (all at once in January) so total return has been even better.

Fairfax	tock price (US$)	increase	increase over past 33 months	S&P500 (US$)	increase	increase over past 33 months
31-Dec-20	$340.94			3,756		
31-Dec-21	$492.13	44%		4,766	27%	
31-Dec-22	$594.12	21%		3,840	-19%	
12-Oct-23	$832.32	40%	144%	4,350	13%	16%

How does this compare to the overall market? The S&P500 is up 16% over the past 33 months.

The performance of Fairfax's share price the past 33 months has been excellent - both in absolute and relative terms. What is a rational investor to do with their shares?

Why SELL of course. At least that is what I would probably have done in the past.

Successful investors need to get two things right: when to buy AND when to sell. Over my investing career, I have been much better at the 'when to buy' decision than the 'when to sell' decision. I have a history of selling my big winners way too early. An example? After a more than 100% gain over a couple of years, I sold most of my concentrated position in Apple in 2016 - right around the time some guy named Warren Buffett was starting to buy shares.

What was my mistake?

My sell decision was focussed primarily on price - not fundamentals.

Apple's underlying business in 2014 and 2015 was getting better each year. After a big gain over 24 months the stock was still cheap when I sold it - and Apple's future prospects were continuing to improve. The crazy part is I knew all of this - I follow my largest positions very closely.

One can conclude that selling Apple in 2016 was a big mistake, right? Not necessarily. One of the things I like about investing is that your mistakes can often lead to your greatest successes. If you learn from them.

What was the lesson I learned? Clearly, I needed to get better at the 'when to sell' part of investing.

Here is what Peter Lynch had to say on the topic of what to do with a stock that has had a big increase in its price. He suggests investors ask themselves the following questions:

- Is 'the story' still good?
- Are earnings continuing to grow?
- Have the fundamentals changed?

<u>If It's Gone This High Already, How Can It Possibly Go Higher?</u>

"If I'd bothered to ask myself, "how can this stock possibly go higher," I would never have bought Subaru after it already had gone up twentyfold. But I checked the fundamentals, realized that Subaru was still cheap, bought the stock, and made sevenfold after that.

"The point is, there's no arbitrary limit to how high a stock go, and if the story is still good, the earnings continue to improve, and the fundamentals haven't changed, "can't go much higher" is a terrible reason to snub a stock. Shame on all those experts who advise clients to sell automatically after they double their money. You'll never get a tenbagger doing that.

"Frankly, I've never been able to predict which stocks will go up tenfold, or which will go up fivefold. **I try to stick with them as long as the story's intact**, hoping to be pleasantly surprised. The success of a company isn't the surprise, but what the shares bring often is."

Peter Lynch - One Up on Wall Street – p. 266 & 267

Let's get back to Fairfax. What has happened with the fundamentals at Fairfax?

Fairfax has three economic engines driving its business:

1. <u>Insurance</u>: Fairfax has grown net premiums written by +250% over the last 8 years. It is on track in 2023 to deliver net premiums written of $24 billion and an underwriting profit of $1.27 bn (94.5CR). Growth in net premiums written in 2024 is expected to be around 12%.

2. <u>Investments - fixed income</u>: Fairfax has navigated the recent spike in interest rates masterfully with their $40 billion fixed income portfolio. In December of 2021, they shortened the average duration to 1.2 years. This action protected their balance sheet. At June 30, 2023, they had pivoted and extended the average duration to 2.4 years. This action has locked in high yields. As a result, interest and dividend income is forecasted to increase to a record $1.9 billion in 2023 and more than $2.5 billion in 2024.

3. <u>Investments - equities</u>: Fairfax's $16.5 billion equity portfolio has been performing well, led by Eurobank and the total return swaps on 1.96 million Fairfax shares.

Most importantly, all of the company's economic engines are performing well at the same time.

Significant asset sales over the past 12 months have been the proverbial icing on the cake: pet insurance (for $1.4 billion), Resolute Forest Products (for $626 million + $183 million CVR) and Ambridge Partners (for $379 million).

The management team at Fairfax has been executing exceptionally well. The company's prospects have rarely looked better.

Let's answer Peter Lynch's three questions for Fairfax:

- 'The story' is still good.
- Earnings are continuing to grow.
- The fundamentals have been getting better.

How do the usual valuation metrics look?

Across all three metrics (PE, P/BV and ROE), and despite the recent run up, Fairfax's stock appears to still offer very good value.

Fairfax Financial (US$)	
Stock Price - Oct 12, 2023	$832
2023 Earnings Estimate	$150
P/E	5.5
Book Value - June 30, 2023	$834
P/BV	1.00
ROE	18%

To conclude, what is a rational investor to do after a 144% gain in 33 months? What would Peter Lynch do?

I think Peter Lynch would stick with this winner. It appears to have the potential to become a 'multi-bagger' in the coming years.

Fairfax: The Big Fish that Got Away?

January 21, 2024

"The stock market is there to serve you and not to instruct you." Warren Buffett

Investors have lots of regrets. Missed opportunities. Not buying a stock that afterwards turns into a big winner. Or selling a winning position way too early. 'The big fish that got away' kind of story.

In 2021, Fairfax's shares returned 44%. An investor looking at Fairfax in early 2022 might have concluded 'dang, missed that one!' and not invested.

In 2022, Fairfax's shares returned 21%. Most stocks got crushed in the bear market of 2022, so Fairfax's performance compared to the averages was exceptional. That same investor, looking at Fairfax in early 2023, might have come to the same conclusion: 'dang, missed that one! For the second year in a row!' and not invested again. The fish story just got bigger.

Well, here we are now in early 2024. How did Fairfax's stock do in 2023? It was up another 55%. Over the past three years shares are up 170%. Investors who did not buy shares (or sold their position too early) over the past three years are left asking themselves what happened? How did they miss out? And what should they do now? The fish story is turning into a whopper of a tale.

Three weeks into 2024 the stock is up another 5%. This puts the total increase at 184% since Dec 31, 2020, making it almost a two-bagger in Peter Lynch's parlance. Fairfax, the 'big fish,' continues to taunt investors.

Fairfax	Share Price (US$)	Increase	Increase over past 3 years	Annual Dividend
Dec 31, 2020	$340.94			$10
Dec 31, 2021	$492.13	44%		$10
Dec 31, 2022	$594.12	21%		$10
Dec 31, 2023	$920.76	55%	170%	$10
Jan 19, 2024	$969.49	5%	184%	$15

What is the lesson to be learned?

By itself, the increase in Fairfax's share price of 184% since Dec 31, 2020, tells you little (nothing?) about Fairfax's valuation today. This is because price (if used by itself) is a terrible valuation tool. Over the past three years, 'investors' who used price as their primary valuation tool for Fairfax have been led astray.

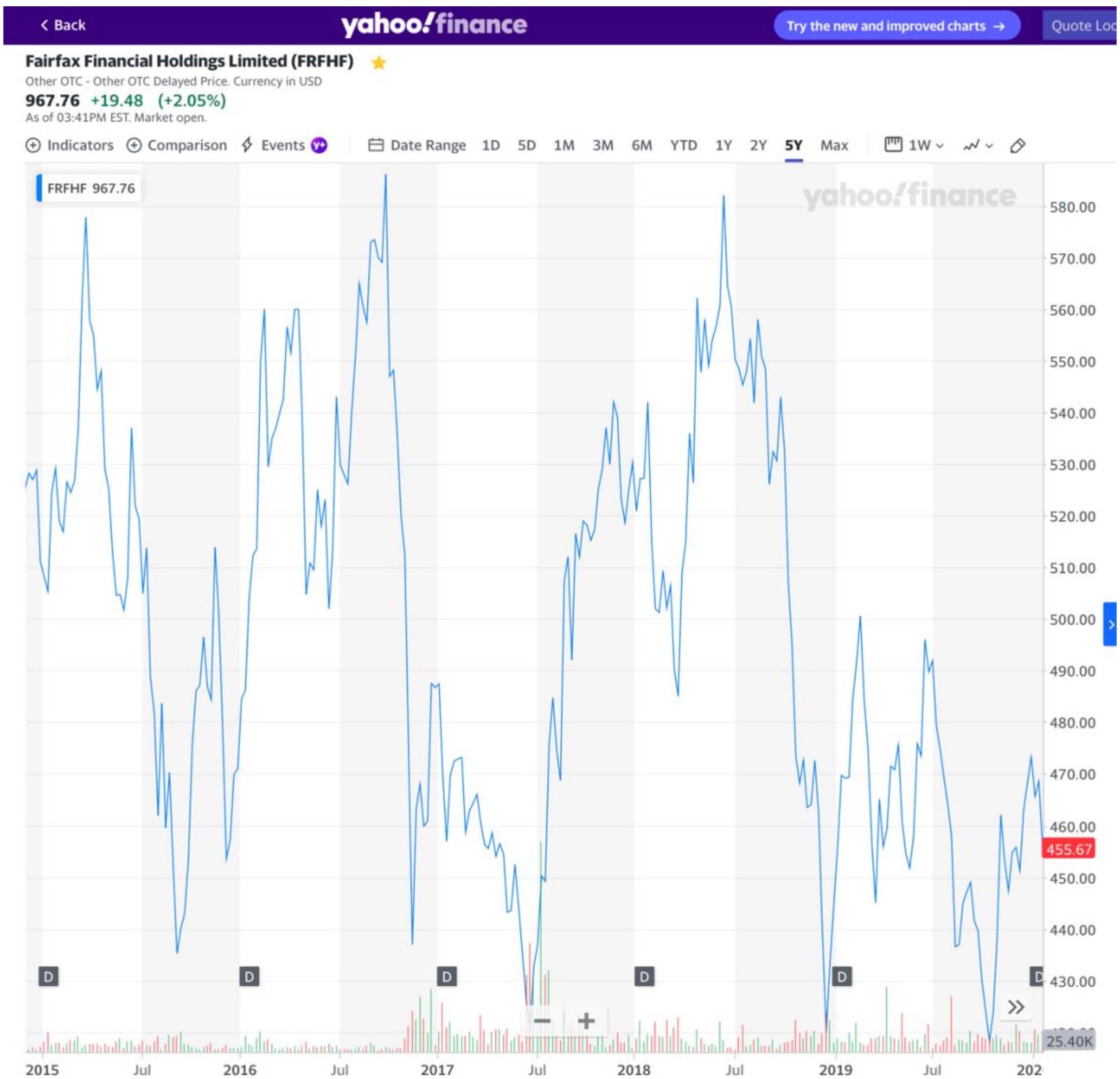
As Buffett teaches us, a stock price exists to serve investors, not to instruct them.

Let's take the discussion in a slightly different direction to see what we can learn.

What happens if we increase the timeframe?

Let's humour ourselves and play the price game for a little longer. But this time with a couple of added twists. Let's zoom out - instead of looking at Fairfax's share price for the past three years, let's look at the share price for the past 9 years. And let's include operating earnings - let's make our analysis a little more robust.

From 2015 to 2019 (right before Covid hit), Fairfax's share price traded in a pretty tight band around US$500. About 50% of the time Fairfax's share price was over $500 and the other 50% of the time it was under $500. So for 5 years straight investors felt Fairfax was worth about US$500/share.



Over this 5-year span, operating earnings at Fairfax averaged about $1.07 billion per year. So from 2015-2019, investors felt $1.07 billion in operating earnings warranted a Fairfax share price of about US$500.

Let's now compare this historical period to today to see what we can learn.

Let's start with the share price. Fairfax's share price closed today at about US$970/share. The stock is up 94% from the average of about $500/share from 2015-2019.

Let's now look at operating earnings. Operating earnings are forecasted to come in at about $4.4 billion for 2023. That is an increase of 305% from the average of $1.07 billion from 2015-2019. My current estimate is for operating earnings to increase in 2024 to about $4.6 billion. Because the share count has come down meaningfully in recent years, this would put operating earnings per share over $200/share in 2024. This is 359% more than the average from 2015-2019 (about $44/share). Importantly, the increase in operating earnings is durable (the average duration of the fixed income portfolio was increased to 3.1 years in October 2023, which locks in interest income for the next couple of years, the largest component of operating income).

Fairfax - Operating Income										
December 31, 2023	**2015**	**2016**	**2017**	**2018**	**2019**	**2020**	**2021**	**2022**	**2023E**	**2024E**
Underwriting profit - ins & reins.	$705	$576	-$642	$319	$395	$309	$801	$1,105	$1,373	$1,270
Interest & dividends	$512	$555	$559	$784	$880	$769	$641	$962	$1,929	$2,250
Share of profit of associates	$173	$24	$201	$221	$170	-$113	$402	$1,015	$1,100	$1,100
Operating income - ins & reins	**$1,390**	**$1,155**	**$118**	**$1,323**	**$1,444**	**$965**	**$1,844**	**$3,082**	**$4,402**	**$4,620**
Per share	$63	$50	$4	$49	$54	$37	$77	$132	$190	$202
Shares Outstanding Dec 31	22.2	23.1	27.75	27.2	26.8	26.2	23.9	23.3	23.2	22.9

Let's put the two together.

Fairfax's stock is up about 90% over the past 9 years. And operating earnings per share - the high quality stuff - is forecasted to be up 359% (over the trend from 2015-2019). High quality earnings have exploded and the stock price has increased modestly.

Valuation: Buffet teaches us that a stock is worth the present value of the cash flows (things like operating earnings) that are expected to be generated in the future.

Conclusion

Looking at Fairfax's share price and using a 3-year time horizon it is easy to conclude the stock must be crazy expensive today. Looking at Fairfax's share price and using a 9-year time horizon (and including operating earnings) it is easy to conclude the stock must be crazy cheap today. How can it be both crazy cheap and crazy expensive at the same time? The answer, of course, is that it can't be both.

Let's circle back to my original comment - using the share price, on its own, as your primary tool to value Fairfax is pretty dumb.

As we begin 2024, that big fish (called Fairfax) is once again staring investors right in the face. And guess what? It's probably going to slip away from them yet again. And in another couple of years, they will think back to today and likely kick themselves. And the story of 'the big fish that got away' will get even bigger.

How do the traditional valuation metrics look today?

Fairfax's stock has a PE of 5.9 (to Yahoo Finance's estimate of 2023 earnings). The ROE for 2023 is tracking to be a little over 20%, which is very good. Price to book value (P/BV) is 1.11, which is very low - and this could come down to around 1.05 when Fairfax reports Q4 results in a few weeks.

Expensive? Really?

Fairfax (US$)	Jan 19, 2024	
Share Price	$969	
2023 Earnings Estimate	$163	Yahoo Finance
P/E	5.9	
	Sept 30, 2023	Dec 31, 2022
Book Value	$877	$657.68
P/BV	1.11	
ROE (average equity)	21%	

What happened in recent years to spike operating earnings so much at Fairfax?

Lots of things. Below is one of them. Fairfax is a P/C insurance company. Net premiums written have grown from $6.1 billion in 2014 to an estimated $26.4 billion in 2024 (my current estimate), an increase of 331% over 10 years. Now over-lay this exceptional growth over 10-straight years with the much more modest increase seen in Fairfax's stock price over the same time frame.

Things that make you go hymmm…

Fairfax: Growth of Net Premiums			
Updated: Dec 31, 2023			
	Net Premiums Written		
31-Dec	$bn	increase	
2014	$6.1		
2015	$7.5		
2016	$8.1		
2017	$10.0		
2018	$12.0	5-year	
2019	$13.3	$7.1	117%
2020	$14.7		
2021	$17.8		
2022	$22.3		
2023E	$23.7	10-year	
2024E	$26.4	$20.3	331%

Chapter 4: P/C Insurance Float

Float – Lost Treasure? An Introduction.

Updated April 7, 2024

Like Indiana Jones, today we are going to set out on an adventure in search of long-lost treasure. Something that most investors appear to have forgotten about. What do the legends tell us? Does it really exist or is it just a myth?

<u>What am i talking about?</u>

P/C insurance float (I'll just call it 'float' moving forward).

Float is such a big (and important) topic we are going to tackle it in a couple of posts. The first post (below) will provide an introduction. The second post will focus on the theory - what it is and why P/C investors should care. The third post will then apply the theory to practice using a real company - Fairfax Financial.

<u>Ancient history</u>

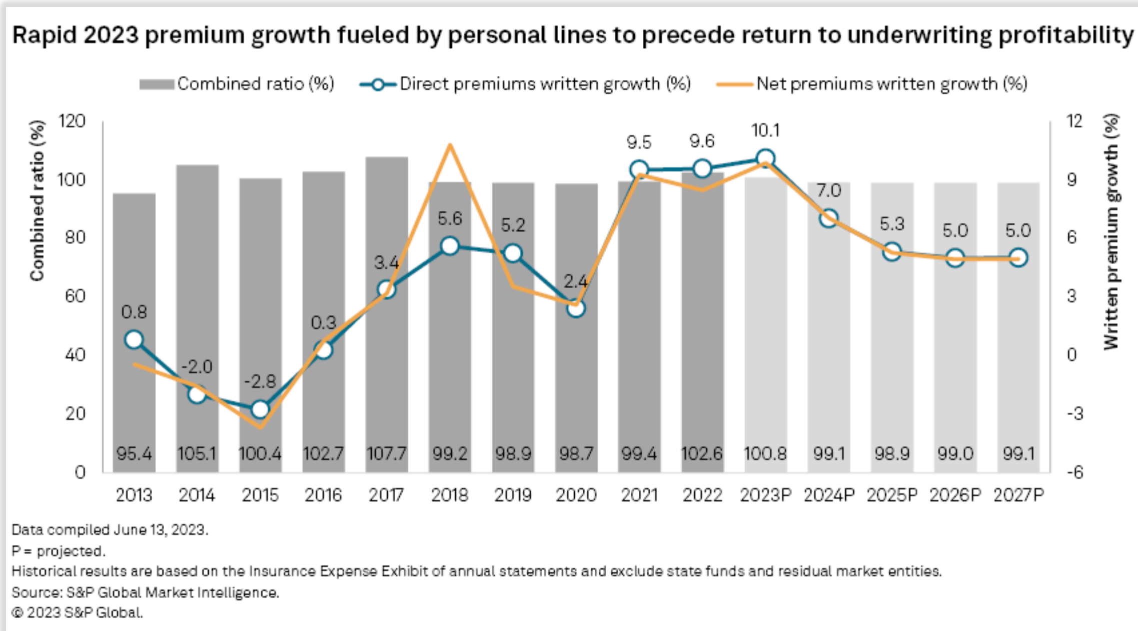
Thirty years ago, talking about float was all the rage for P/C investors. Read old articles on investing in P/C insurance companies and a discussion of float will usually be front and center. And the champion of float from that era was, of course, Warren Buffett and his company Berkshire Hathaway.

<u>So, what happened?</u>

Why has float apparently settled into the dustbin of history and become a relic of the past?

1. Due to competitive insurance markets, industrywide underwriting profit has remained low for the past decade. Until recent years, top line organic growth had slowed to a crawl.
2. Returns on investments fell: P/C insurers put most of their investments into fixed income instruments. In their battle with deflation, global central banks took interest rates all the way into negative territory. The US 10-year treasury traded at a yield below 0.60% in August of 2020 and traded with a yield below 1.5% for much of 2021.

S&P Global: US P/C Insurance Market Report



Float lost its value

Breaking even on underwriting for a decade while returns on investments plummeted made having float far less valuable than at any point in recent history.

Another small factor: over the years, P/C insurance has become a much smaller part of Berkshire Hathaway's business model. What did Buffett have to say about float in his 2022 letter to shareholders? Float is mentioned 4 times in one short paragraph - telling investors to go somewhere else if they wanted to learn more. Does this sound important to you? So 'float' also lost its biggest cheerleader.

Does this mean… Float is dead? Long live float?

No, of course not. Just because float is no longer appreciated (or followed) doesn't mean it doesn't matter. In fact, for those paying attention, the world has changed again. The conditions that made float a big deal 30 years ago have returned:

1. Insurance has been in a hard market since about Q4 of 2019 - above average insurance companies are seeing significant top-line growth (supply of float) and improving underwriting results (cost of float) over the past four years.

2. Global central banks now have an inflation fight on their hands - and 'higher for longer' is becoming the new mantra for interest rates. Fixed income yields have spiked higher across the curve. The 10-year US treasury closed recently with a yield of 4.70%, a level where it last traded at in 2007. As a result, returns on float are improving greatly.

Both of these developments make having float today <u>extremely</u> valuable.

Except remember… pretty much everyone has forgotten about float.

What's old will be new again.

Well, my guess is this is about to change. I think investors are going to get interested in float again.

What is going to cause the change?

A new generation of investors are about to discover something Warren Buffett hit on when he bought National Indemnity back in 1967: float, under certain conditions, can be a license to print money. Those 'certain conditions' have returned. And in recent years a few insurance companies have started up the printing presses and are now starting to print money.

Float – What Can Warren Buffett Teach Us?

Updated April 7, 2024

P/C insurance float: the basics

Float is deceptive. It is kind of like compound interest as a concept. It is easy to define but very hard to actually understand.

Who better to teach us about P/C insurance float than the old master, Warren Buffett himself.

Float: the basic building block to use to evaluate a P/C insurance company

Back in the 1990's, Warren Buffett was using P/C insurance as the core engine to drive Berkshire Hathaway's profit growth. GEICO was purchased in 1996 and General Re was purchased in 1998. Given the importance of P/C insurance to Berkshire Hathaway, Buffett provided the following as a guide to help shareholders understand P/C insurance as an investment.

> "With the acquisition of General Re — and with GEICO's business mushrooming — it becomes more important than ever that you understand how to evaluate an insurance company. The key determinants are:
>
> 1.) the amount of float that the business generates;
> 2.) its cost; and
> 3.) most important of all, the long-term outlook for both of these factors."
>
> *Warren Buffett – Berkshire Hathaway 1998AR*

Well, Warren appears to be saying float is the most important thing to understand when evaluating an insurance company. Interesting, given how little press float gets today from analysts and investors.

What is float?

> "To begin with, float is money we hold but don't own. In an insurance operation, float arises because premiums are received before losses are paid, an interval that sometimes extends over many years." *Warren Buffett – Berkshire Hathaway 1998AR*

Float is money a P/C insurer has that it can use to invest. It is an asset (benefit) but it is a liability (not equity). It is kind of like a very sticky deposit at a bank (a deposit is also a liability for a bank).

Because float is a liability, it is also leverage. Like all leverage (i.e. debt), float can be both good or bad - and this depends on the cost paid over time to hold the float.

What is the cost of float?

> "Typically, this pleasant activity (the P/C insurance business) carries with it a downside: The premiums that an insurer takes in usually do not cover the losses and expenses it eventually must pay. That leaves it running an "underwriting loss," which is the cost of float. **An insurance business has value if its cost of float over time is less than the cost the company would otherwise incur to obtain funds.** But the business is a lemon if its cost of float is higher than market rates for money." *Warren Buffett – Berkshire Hathaway 1998AR*

Underwriting determines the 'cost' of float.

This point is critical. Over time, if an insurer can produce an underwriting profit on its insurance business that means the cost of its float is actually a benefit - that is better than free. **That means the insurer is actually getting paid to hold the float.**

Float is a pile of money that an insurance company can actually earn two income streams from: underwriting (if float is obtained at a benefit) and investing.

Sounds like Buffett was on to something when he decided to invest in P/C insurance companies.

To summarize: according to Buffett, a good P/C insurance company:

1. Has a large amount of float.
2. Is a good underwriter - is able to generates the float at a favourable cost (ideally a benefit).
3. Has a good long term track record - of both growing float and as a solid underwriter.

Buffett's secret sauce: P/C insurance float

Buffett's genius has really been two-pronged:

- Use P/C insurance float as an ever-increasing low cost (free) source of capital/leverage to push profits higher.
- Reinvest these growing profits into great companies/equities outside of insurance – these businesses then generate new income streams.
- Both P/C insurance and non-insurance operating companies/equities become compounding machines over time.

OK. So. there is a quick review of float, explained with the help of Warren Buffett.

To help us understand float even better, let's look at it now from a balance sheet perspective.

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Float and the balance sheet

Let's create an imaginary insurance company - called Random P/C Insurance Co - and create a fictitious balance sheet.

Our company has $80 billion in assets, with $60 billion in liabilities and $20 billion in common shareholders' equity. Of the total liabilities of $60 billion, float is $30 billion. The summary of the balance sheet is below:

Random P/C Insurance Company				
Consolidated Balance Sheet			A - L = E	
	US$bn			
Assets	$80.0			
Liabilities	$60.0	→	$30	Float
Common Equity	$20.0			

We are also going to assume common shareholders' equity = book value.

We are going to make up more numbers below. We are using numbers that make our calculations easy. Please don't focus too much on the exact numbers. Instead, focus on the information they are trying to convey - especially about leverage.

Cost of float

Let's assume our insurance company is a slightly above average underwriter with a combined ratio (CR) of 96 - this translates into a 'benefit' of float (better than free - our company is actually getting paid to hold their float).

Return on investments (which includes float)

Let's assume our insurance company is above average in terms of the return it earns from its total investments (which includes float) - let's assume it earns 8% on average.

We are also going to assume there are no taxes.

The return of Random P/C Insurance Co

When we put the two together, we get:

1. Benefit of float (CR of 96)
2. Return on investments = 8%

Let's assume Random P/C Insurance Co earns a total return of 10% on its float.

This means our insurance company is earning the following:
- $30 billion float x 10% = $3 billion.

Can we calculate the actual leverage provided by the float?

Yes. Total earnings from float of $3 billion will flow though the income statement and increase retained earnings, which will then flow through to the balance sheet and increase both assets and common shareholder equity by $3 billion.

So, a return from float of 10% results in an increase in common shareholders' equity of 15%.

Random P/C Insurance Company				
Return generated by float only			**YOY Change**	
	Year 1	**Year 2**	**$**	**%**
Assets ($bn)	$80.0	$83.0		
Liabilities	$60.0	$60.0		
Common Equity	$20.0	$23.0	$3.0	15%

The leverage can be calculated as follows: total float / common shareholders' equity.

In our example:
- float of $30 billion / common shareholders' equity of $20 billion = 1.5 x leverage

Float leverage of 1.5 times, means:			
Return on float of:	5%	10%	15%
Delivers Return on Equity (ROE)	7.5%	15%	22.5%

Common equity, debt and total investments

The above increase in common shareholders' equity was driven solely by float. A company is also going to generate earnings from its common shareholders' equity - the funds provided by shareholders. Perhaps it also uses a little debt to generate even more earnings. Any returns generated by its other investments (those other than float) need to be added to the numbers above.

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Below, Buffett summarizes how float fits into the big picture

"In more years than not, our cost of funds has been less than nothing. This access to "free" money has boosted Berkshire's performance in a major way.

"Any company's level of profitability is determined by three items:

1. what its assets earn;
2. what its liabilities cost; and
3. its utilization of "leverage" - that is, the degree to which its assets are funded by liabilities rather than by equity.

"Over the years, we have done well on Point 1, having produced high returns on our assets. But we have also benefitted greatly - to a degree that is not generally well-understood - because our liabilities have cost us very little. An important reason for this low cost is that we have obtained float on very advantageous terms. The same cannot be said by many other property and casualty insurers, who may generate plenty of float, but at a cost that exceeds what the funds are worth to them. In those circumstances, leverage becomes a disadvantage.

"**Since our float has cost us virtually nothing over the years, it has in effect served as equity.** Of course, it differs from true equity in that it doesn't belong to us. **Nevertheless, let's assume that instead of our having $3.4 billion of float at the end of 1994, we had replaced it with $3.4 billion of equity.** Under this scenario, we would have owned no more assets than we did during 1995. We would, however, have had somewhat lower earnings because the cost of float was negative last year. That is, our float threw off profits. And, of course, to obtain the replacement equity, we would have needed to sell many new shares of Berkshire. **The net result - more shares, equal assets and lower earnings - would have materially reduced the value of our stock. So you can understand why float wonderfully benefits a business - if it is obtained at a low cost.**"

Warren Buffett – Berkshire Hathaway 1995AR

Float is better than equity?

This question is a bit of a mind bender. Because of its unique 'cost' (i.e. low cost or even a benefit), in the past Buffett has said that he views float as being better than equity.

> "Since 1967, when we entered the insurance business, our float has grown at an annual compounded rate of 21.7%. Better yet, it has cost us nothing, and in fact has made us money. **Therein lies an accounting irony: Though our float is shown on our balance sheet as a liability, it has had a value to Berkshire greater than an equal amount of net worth would have had.**"
>
> *Warren Buffett – Berkshire Hathaway 1997AR*

Well, suggesting float is better than equity is perhaps a bridge too far. However, I think we can conclude that float matters a great deal. Especially today in a high interest rate world.

Conclusion

OK. So now we know what float is and the key metrics to use to evaluate P/C insurers. Who should we start with? That is an easy question to answer. In our next post, we will do a deep dive on float at Fairfax Financial to see what we can learn.

YouTube Video Explaining P/C Insurance Float

> How Warren Buffett Achieves Great Returns Every Year - Advantages of Insurance Float
>
> https://youtu.be/XCL0GRPQKAk

Fairfax Financial and Float - A Deep Dive

April 7, 2024

In my last post I reviewed the world of P/C insurance float, largely through the writings of Warren Buffett - a pretty knowledgeable guy on the subject. In this post we are going to pivot to the real world and try and apply what we learned to Fairfax Financial.

Summary of the topics on float and Fairfax that we will explore in this post:

- A quick review of financial leverage
- Size of float
- Leverage provided by float
- Growth of float
- Cost of float
- Returns being achieved on float
- Summary

A quick review of financial leverage

Balance Sheet: Assets (A) = Liabilities (L) + Equity (E)

To grow (increase assets) a company can issue a liability like debt (borrow) or equity (shares).

Borrowing (a liability) is simply a way to use other people's money to finance growth / business activities. Using borrowed money to grow/invest is a financial strategy referred to as leverage.

Why use leverage to grow? To increase the return on equity. If equity stays constant but a firm can grow assets, which in turn grows earning, that will result in higher return on equity.

What is the rub? There is a cost to borrow, which is the interest rate charged on the loan. Borrowing has a cost. And today, with interest rates elevated, the cost is high (compared to recent history).

What does this have to do with P/C insurance companies?

P/C insurance companies are unique animals. Through the course of their business operations, they generate something called float. Float is the money held by insurance companies when they receive premiums that has not yet been paid out to claimants.

Like debt, float is other peoples' money so it is technically a liability. Like debt, float can be used to purchase investments on the asset side of the balance sheet. The investments purchased with float will then grow total earnings, which results in a higher return on equity for the company.

Growing float (L) = growing investments (A) = growing earnings = growing equity (E) = higher return on equity (ROE).

What is the rub? There is a cost to float and it is determined by underwriting (combined ratio). If an insurer is able to generate an underwriting profit over time, the cost of float is free (actually better than free… the 'cost' is a benefit).

So, for P/C insurance companies float provides a (potential) free source of capital that can be invested elsewhere to boost earnings and return on equity (ROE).

Let's now see how all of this applies to Fairfax.

How much float does Fairfax have?

At December 31, 2023, Fairfax had $35.1 billion in total float. However, to make our analysis more meaningful, we need to make 2 adjustments to this number:

1. Remove float from runoff - Fairfax separates runoff when reporting underwriting results so to be consistent we will remove runoff float from our analysis. In this post we will only be looking at float for insurance/reinsurance at Fairfax.
2. remove minority interests - small amounts of Allied World, Odyssey, Brit and International are owned by minority shareholders. We also adjust float to account for this. By removing the share of float that accrues to minority shareholders we are left with the amount of float that accrues to Fairfax's common shareholders, which is really the number we care about.

After making the 2 adjustments outlined above, at December 31, 2023, Fairfax had $30.2 billion in float working for common shareholders (I am going to call this 'adjusted float' in the remainder of this post.) Adjusted float was $1,313/share.

Fairfax: Adjustments To Total Float	
December 31, 2023	
	Total
Total Float ($bn)	$35.1
Less Runoff Float	-$1.7
Insurance and Reinsurance Float	$33.4
Less Minority Interests	-$3.2
Adjusted Float ($bn)	**$30.2**
Per Common Share (23m)	**$1,313**

Fairfax Float: Insurance and Reinsurance Adjusted for Minority Interests								
Dec 31, 2023								
	NB	**Odyssey**	**Crum**	**Zenith**	**Brit**	**Allied**	**Other**	**Total**
Fairfax Owns	100%	90%	100%	100%	86.2%	83.4%	90%	**91%**
Ins + ReIns Float	$2.9	$8.9	$5.0	$1.1	$4.1	$8.4	$3.0	**$33.4**
Minority Share	$0.0	$0.9	$0.0	$0.0	$0.6	$1.4	$0.3	**$3.2**
Fairfax Share	**$2.9**	**$8.0**	**$5.0**	**$1.1**	**$3.5**	**$7.0**	**$2.7**	**$30.2**

Now that we know the size of Fairfax's float, let's now look at it in relation to Fairfax's total balance sheet.

<u>What is the leverage provided by Fairfax's adjusted float?</u>

Common shareholders' equity at Fairfax was $21.6 billion at Dec 31, 2024. As we just learned above, adjusted float is $30.2 billion. **Adjusted float is 1.4 x bigger than common shareholders' equity.**

The leverage is 1.4 times (adjusted float of $30.2 / common shareholders' equity of $21.6). That means every 1% gain from float = 1.4% gain in common shareholders' equity (ROE = 1.4%)

So, if float delivers an 8% return to Fairfax that will boost common shareholder's equity by 11.2% (deliver an ROE = 11.2%) <u>all by itself</u>.

Fairfax			A - L = E	
Consolidated Balance Sheet				
Dec 31, 2023	US$bn		Insurance and Reinsurance	
Assets	$92.0		Fairfax's Share	
Liabilities	$64.3		$30.2	Adjusted Float
Equity	$27.7			
			Adj Float to Common Equity	
Common Shareholders' Equity	$21.6		1.40	Leverage

<u>How much has total float grown in recent years at Fairfax?</u>

Please note, in this section we will use the float numbers for insurance/reinsurance (runoff is excluded). However, I did not separate out minority interests. It would have been a lot of work and it wouldn't have materially changed the conclusions (the growth numbers) - which is what we care about here.

The float of insurance/reinsurance has been growing rapidly at Fairfax for many years:

- From 2014 to 2023 (9 years), float grew from $11.6 to $33.4 billion, an increase of 188%.
    - This is a CAGR of 12.5%/year.
- From 2015-2017, growth was fuelled primarily by acquisitions (Brit, international and Allied World).
- From 2020-2023, growth was fuelled primarily by organic growth (insurance hard market).
- 2024 should see solid growth in float driven by continuation of the hard market.

The management team at Fairfax has done a fantastic job of growing float over the past 9 years. And the prospects for continued growth look good.

Fairfax - Insurance and Reinsurance			
April 7, 2024			
Insurance + Reinsurance Float			
31-Dec	$bn	change	/share
2014	$11.6		$547
2015	$13.7	18%	$617
2016	$13.8	1%	$597
2017	$20.2	46%	$727
2018	$19.7	-2%	$724
2019	$20.6	5%	$769
2020	$22.7	10%	$866
2021	$25.9	14%	$1,084
2022	$29.6	14%	$1,270
2023	$33.4	13%	$1,452
2024E	$35.0	5%	$1,542

What is the cost of float? What is the trend?

Like borrowing money, float is a liability. Like all leverage (i.e. debt), float can be both good or bad - and this depends on the cost paid over time to hold the float.

The 'cost' of float is measured by looking at underwriting results and the combined ratio. Fairfax excludes runoff when it reports underwriting results and the combined ratio (CR) so we can use their numbers in this section.

Summary:

- From 2014-2023 (9 years), the CR at Fairfax averaged 95.5%
    - From 2018-2020, the CR ticked higher and averaged 97.3%
    - For 2021-2023, the CR ticked lower and averaged 94.3%

- For 2024, my current estimate for the CR is 95%

Fairfax has consistently earned an underwriting profit on its adjusted float. This means that is has been able to secure $30.2 billion in adjusted float on very favourable terms. In fact, the 'cost' of float is better than free - it is a benefit. I know, that sounds crazy - but it is true.

This is why Buffett has said in the past that he views float as being more valuable than a similar amount of equity. That statement is a real mind bender.

What is driving the improvement in the combined ratio in recent years?

My guess is two factors are driving the improvement:

1. The hard market in insurance (began in Q4, 2019) - resulting in higher prices and better terms and conditions.

2. Slow incremental improvement in the quality of Fairfax's collective insurance businesses - resulting in better underwriting. This is being driven by Andy Barnard and the leaders of the various insurance companies.

Fairfax - Insurance and Reinsurance					(Cost)
April 7, 2024				Comb	Benefit
Insurance + Reinsurance Float				Ratio	of
31-Dec	$bn	change	/share	CR	Float
2014	$11.6		$547	90.8	9.2%
2015	$13.7	18%	$617	89.9	10.1%
2016	$13.8	1%	$597	92.5	7.5%
2017	$20.2	46%	$727	106.6	-6.6%
2018	$19.7	-2%	$724	97.3	2.7%
2019	$20.6	5%	$769	96.9	3.1%
2020	$22.7	10%	$866	97.8	2.2%
2021	$25.9	14%	$1,084	95.0	5.0%
2022	$29.6	14%	$1,270	94.7	5.3%
2023	$33.4	13%	$1,452	93.2	6.8%
2024E	$35.0	5%	$1,542	95.0	5.0%

So, float has been growing at 12.5% per year for the past 9 years. And the 'cost' has actually been better than free - a 'benefit' - over the same time frame.

But the story gets even better. Why? Return.

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<u>What is the return Fairfax has been earning on its float?</u>

Fairfax has $30.2 billion in adjusted float that is invested and earning a return for shareholders.

For reference, the total investment portfolio at Fairfax was about $65 billion at Dec 31, 2023. Adjusted float of $30.2 billion represents 46.5% of total investments. It is significant.

In this section we are going to look at Fairfax's return on total investments. We are not going to try and break out Fairfax's returns specific to float (which is a part of total investments). Again, we are coming at this analysis at a very high level. If we subscribe a lower than average return to float (by assuming it is more skewed to short-term fixed income investments) we would then need to attach a higher return to Fairfax's non-float investments to get to the correct average number.

Instead, we are going to keep our analysis simple and use Fairfax's average return on total investments as a very rough estimate for what is being earned on adjusted float.

From 2018 to 2022 (5 years), Fairfax's total return on investments averaged about 5.2% per year. Not surprisingly, a big drag was the fixed income portfolio. Fairfax's interest and dividend income (a reasonable proxy for the return on the fixed income portfolio) delivered an average return of about 2.4% from 2018 to 2022.

Today? In 2023, Fairfax earned a total return of 9.6% on its investment portfolio. That is 85% more than the 5-year average of 5.2% from 2018-2022. That is a meaningful increase (big understatement!).

What are the biggest drivers of the increase in total return?

- Interest and dividend income delivered a return of 4.4% in 2023.
- Equity holdings also performed well in 2023.
- Since 2018, Fairfax has been making very good capital allocation decisions - with the benefits increasingly showing up in reported results.

What about future returns?

Fairfax has extended its fixed income portfolio from 1.2 years at Dec 31, 2021 to more than 3 years at December 31, 2023. This locks in higher interest rates for the next 3 to 4 years.

It seems reasonable to expect the management team at Fairfax to continue to make good capital allocation decisions.

Bottom line, Fairfax looks well positioned to continue to deliver strong investment returns moving forward. My current estimate has Fairfax earning a return of about 7.4% on its growing investment portfolio in 2024 and 2025.

Fairfax - Insurance and Reinsurance					**(Cost)**	**Total**	**Only**	**Effective**
April 7, 2024				**Comb**	**Benefit**	**Return**	**Interest**	**Shares**
Insurance + Reinsurance Float				**Ratio**	**of**	**All**	**And**	**Out-**
31-Dec	**$bn**	**change**	**/share**	**CR**	**Float**	**Investments**	**Dividends**	**standing**
2014	$11.6		$547	90.8	9.2%		2.0%	21.2
2015	$13.7	18%	$617	89.9	10.1%		2.3%	22.2
2016	$13.8	1%	$597	92.5	7.5%		2.5%	23.1
2017	$20.2	46%	$727	106.6	-6.6%		1.8%	27.8
2018	$19.7	-2%	$724	97.3	2.7%	2.5%	2.8%	27.2
2019	$20.6	5%	$769	96.9	3.1%	8.5%	3.1%	26.8
2020	$22.7	10%	$866	97.8	2.2%	1.1%	2.4%	26.2
2021	$25.9	14%	$1,084	95.0	5.0%	10.7%	1.5%	23.9
2022	$29.6	14%	$1,270	94.7	5.3%	2.5%	2.3%	23.3
2023	$33.4	13%	$1,452	93.2	6.8%	9.6%	4.4%	23.0
2024E	$35.0	5%	$1,542	95.0	5.0%	7.4%	4.7%	22.7

Ok. Let's try and summarize everything.

What have we learned about Fairfax and its float?

1. Adjusted float is $30.2 billion. It has been compounding at 12.5% per year for the past 9 years.
2. 'Cost' of float is actually a benefit - and the benefit has increased in recent years.
3. The average return Fairfax is earning on its total investments came in at 9.6% in 2023 and it is estimated to be 7.4% in 2024 and 2025, up from an average of 5.2% from 2018-2022.

When looking at float, all three of the most important metrics are moving to the benefit of Fairfax and its shareholders. It is large and increasing in size. It is being obtained at a very favourable cost - better than free. And the return being achieved on its investments has spiked and the higher number looks sustainable.

So how does float fit into Fairfax's valuation today?

This is where things get interesting.

Fairfax's stock is trading today at 1.15 x book value (Dec 31, 2023). Mr. Market is saying that Fairfax is worth slightly more than its book value.

Fairfax (US$)		
Share Price	$1,079	March 31, 2024
Book Value	$940	Dec 31, 2023
P/BV	1.15	

What about float?

Mr. Market appears to be assigning little value to Fairfax's adjusted float of $1,313/share ($30.2 billion) at Dec 31, 2024. Remember, back in 1995 Buffett said that he felt float was better to have than an equal amount of equity.

Assigning a very low value to adjusted float might have made some sense when interest rates were very low. But in the current environment, where interest rates are high and likely to remain high, this makes no sense. Mr. Market appears to be significantly underestimating the earnings power of Fairfax.

BERKSHIRE HATHAWAY INC.
PROPERTY/CASUALTY INSURANCE*

Our property/casualty ("P/C") insurance business has been the engine propelling Berkshire's growth since 1967, the year we acquired National Indemnity and its sister company, National Fire & Marine, for $8.6 million. Today, National Indemnity is the largest P/C company in the world as measured by net worth. Insurance is a business of promises, and Berkshire's ability to honor its commitments is unmatched.

One reason we were attracted to the P/C business was the industry's business model: P/C insurers receive premiums upfront and pay claims later. In extreme cases, such as claims arising from exposure to asbestos, or severe workplace accidents, payments can stretch over many decades.

This collect-now, pay-later model leaves P/C companies holding large sums – money we call "float" – that will eventually go to others. Meanwhile, insurers get to invest this float for their own benefit. Though individual policies and claims come and go, the amount of float an insurer holds usually remains fairly stable in relation to premium volume. Consequently, as our business grows, so does our float. And *how* it has grown, as the following table shows:

Year	*Float (in millions)*
1970	$ 39
1980	237
1990	1,632
2000	27,871
2010	65,832
2020	138,503
2021	146,701
2022	164,109

We may in time experience a decline in float. If so, the decline will be *very* gradual – at the outside no more than 3% in any year. The nature of our insurance contracts is such that we can *never* be subject to immediate or near-term demands for sums that are of significance to our cash resources. That structure is by design and is a key component in the unequaled financial strength of our insurance companies. That strength will *never* be compromised.

If our premiums exceed the total of our expenses and eventual losses, our insurance operation registers an underwriting profit that adds to the investment income the float produces. When such a profit is earned, we enjoy the use of free money – and, better yet, get *paid* for holding it.

For the P/C industry as a whole, the financial value of float is now far less than it was for many years. That's because the standard investment strategy for almost all P/C companies is heavily – and *properly* – skewed toward high-grade bonds. Changes in interest rates therefore matter enormously to these companies, and during the last decade the bond market has offered pathetically low rates.

Consequently, insurers suffered, as year by year they were forced – by maturities or issuer-call provisions – to recycle their "old" investment portfolios into new holdings providing much lower yields. Where once these insurers could safely earn 5 cents or 6 cents on each dollar of float, they now take in only 2 cents or 3 cents.

Some insurers may try to mitigate their loss of revenue by buying lower-quality bonds or non-liquid "alternative" investments promising higher yields. But those are dangerous games and activities that most institutions are ill-equipped to play.

Berkshire's situation is more favorable than that of insurers in general. Most important, our unrivaled mountain of capital, abundance of cash and a huge and diverse stream of non-insurance earnings allow us far more investment flexibility than is generally available to other companies in the industry. The many choices open to us are always advantageous – and sometimes have presented us with major opportunities.

Our P/C companies have meanwhile had an excellent underwriting record. Berkshire has now operated at an underwriting profit for 18 of the last 20 years, the exceptions being 2017 and 2022. In 2017 our pre-tax loss was a whopping $3.2 billion. In 2022 the loss was minimal. For the entire 20-year span, our pre-tax gain totaled $29.2 billion.

That record is no accident: Disciplined risk evaluation is the daily focus of our insurance managers, who know that the rewards of float can be drowned by poor underwriting results. All insurers give that message lip service. At Berkshire it is a religion, Old Testament style.

As I have repeatedly done in the past, I will emphasize now that happy outcomes in insurance are far from a sure thing: Danger always lurks.

Mistakes in assessing insurance risks can be huge and can take many years – even decades – to surface and ripen. (Think asbestos.) A major catastrophe that will dwarf hurricanes Katrina and Ian *will* occur – perhaps tomorrow, perhaps many decades from now. "The Big One" may come from a traditional source, such as wind or earthquake, or it may be a total surprise involving, say, a cyber attack having disastrous consequences beyond anything insurers now contemplate. When such a mega-catastrophe strikes, Berkshire will get its share of the losses and they will be big – *very* big. Unlike many other insurers, however, handling the loss will not come close to straining our resources, and we will be eager to *add* to our business the next day.

**** Reproduced from Berkshire Hathaway Inc. 2019 Annual Report and updated through 2022***

Chapter 5: Capital Allocation

What kind of an investor is Fairfax?

Updated: October 12, 2023

To the question "What kind of an investor is Fairfax?" most people would answer "value investor." That is the right answer but it doesn't really tell us much. What kind of a value investor?

To answer this question, we are going to look at what Fairfax has been doing for the past three years. What have they actually been buying? What can we learn?

But first, let's set the table.

1.) "The single most important thing (when investing in the stock market)… is to <u>know what you own.</u>" *Peter Lynch*

The problem with Peter Lynch is he says so many smart (and funny) things that his 'most important thing' gets lost in the shuffle. This is the 'north star' of everything else he writes. From this naturally flows another of Peter Lynch's nuggets of gold.

2.) "The best stock to buy is the one you already own." *Peter Lynch*

This makes intuitive sense. You have already done the research on the stocks you own. You know 'the story' and you like it (that's why you own it). Assuming the fundamentals are still solid, then buying more should be a no brainer. Buffett takes this idea a little further with the following quote:

3.) "Diversification may preserve wealth, but concentration builds wealth." *Warren Buffett*

The idea is to invest with conviction around your best ideas. Especially if the stock is on sale. This leads us to our next point.

4.)"'The three most important words in investing are margin of safety." *Warren Buffett*

Ben Graham introduced 'margin of safety' as the central concept of investing in Chapter 20 of his book, The Intelligent Investor. The idea is to only purchase stocks when they are trading at a big discount to their intrinsic value (buy something for $0.50 that is worth $1.00). This approach limits your downside if you are wrong and it provides significant upside if you are right.

What do we get when we combine these four points?

Often, your best investment is to simply buy more of something you already own - especially when it is on sale.

One added twist:

> 5.) "If you search world-wide, you will find more bargains and better bargains than by studying only one nation." *John Templeton*

Invest wherever in the world the best opportunities are.

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What does all of this have to do with Fairfax?

Well, guess what Fairfax has been doing for the past 3 years? It has invested close to $6.2 billion in stuff it already owns. Yes, during this time Fairfax has been investing in new ventures but the amount spent is much smaller. In short, Fairfax has been feasting at the buffet of companies it already owns.

Let's review the actual investments that Fairfax has been making the past 3 years (Aug 2020 to Aug 2023) that fit this theme to see what we can learn.

1.) Buy Fairfax stock: amount spent $2.26 billion

- Total Return Swap (late 2020/early 2021): exposure to 1.96mn Fairfax shares at $372/share
    - Total investment = $732 million (notional)
    - This investment has delivered a gain of $900 million so far (before carrying costs).

Fairfax Total Return Swaps		**FFH share price**	**TRS market value**	**TRS cumulative increase in value**		
1.96	mill shares			**$**	**%**	**per share**
Late 2020/Early 2021		$373	$731	Value at at inception		
October 12, 2023		$832	$1,631	$900	123%	$39

- Dutch Auction (Dec 2021): purchased 2 million Fairfax shares at $500/share
    - Total investment = $1 billion
- NCIB (June 2020-June 2023): purchased an additional 1.133 million shares at $490/share
    - Total investment = $535 million

Fairfax - Total Reduction In Share Count Last 3 Years				
Date	Effective Shares Outstanding million	Share Reduction million	Avg Cost Per Share	Total Cost billion $
Jun 30, 2020	26.335			
Dec 31, 2020	26.177	0.159	$298	$0.047
Dec 31, 2021	23.866	2.311	$490	$1.132
Dec 31, 2022	23.325	0.540	$509	$0.275
Jun 30, 2023	23.202	0.123	$651	$0.080
Totals	**12%**	**3.133**	**$490**	**$1.535**

<u>Let's put all 3 together: FFH TRS + Dutch Auction + NCIB</u>

Over the past 3 years Fairfax has 'purchased' 5.09 million shares of Fairfax (19.3% of effective shares outstanding) at a total 'cost' of $2.3 billion, or an average of $445/share. With shares trading today at $832, the value creation for Fairfax shareholders has been very roughly about $2 billion.

For Fun, Let's Add In The Total Return Swap Position	Shares Purchased	Avg Cost Per Share	Total US$ billion
Total Shares Repurchased	3.133	$490	$1.535
Total Return Swaps	1.960	$372	$0.729
Total Shares 'Purchased'	5.093	$445	$2.264
	19.3%		
		Per Share	Total US$ billion
Fairfax Share Price Oct 12, 2023		$832	
3 Year Value Creation for Shareholders		**$387**	**$1,973**

Share buybacks should be done when shares are trading below intrinsic value. Fairfax bought back shares - and in significant quantities – when they were trading well below intrinsic value. Value investing at its best. And exceptional capital allocation.

<u>Who does this string of purchases remind you of?</u>

Not Lynch, Buffet or Graham. Who then? Henry Singleton. Who is this guy?

> "I mentioned to you last year that we are focused on buying back our shares over the next ten years as and when we get the opportunity to do so at attractive prices. Henry Singleton from Teledyne was our hero as he reduced shares outstanding from approximately 88 million to 12 million over about 15 years." *Prem Watsa – Fairfax 2018AR*

At the time, many laughed at Prem for making this comment. I don't think these same people are laughing at Prem today.

2.) Increase Ownership of Insurance Businesses - Buy Out Partners = $1.9 billion

Insurance is the most important economic engine that Fairfax has. Top line growth in the insurance businesses is important to sustainable profit growth at Fairfax over time. And profitability is what determines the share price over the medium to long term.

Fairfax is slowly and methodically taking out the minority partners in its insurance companies. They spent $1.9 billion over the past 3 years doing this. As a result, they own a larger share of the growing future earnings of these high quality companies.

Fairfax - Investments in Insurance Holdings			
June 2020 - June 2023		Amount	June 2020 - June 2023
Year	Holding	US$	Comments
2021	Eurolife	$143	Inreased ownership from 50 to 80%
2021	Singapore Re	$103	Increased ownership from 28.1 to 100%
2022	Allied World	$733	Increased ownership from 70.9 to 82.9%
2023	Gulf Ins Group	$860	Increased ownership from 43.4 to 90%
2023	Allied World	$31	Increased ownership from 82.9 to 83.4%
	Total Insurance	**$1,870**	

Note: the GIG purchase is expected to close in Q4, 2023.

3.) Increase Ownership of Equity investments:

- Consolidated Equities = $0.67 billion

These are the equity investments that Fairfax exerts a great deal of control over. They invested $666 million the past three years. The big purchase was taking Recipe private – Fairfax was able to buy the stock when it was trading at a pandemic discount.

Fairfax - Investments in Non-Insurance - Consolidated Equities			
June 2020 - June 2023		Amount	
Year	Holding	US$	Comments
2021	Thomas Cook	$60	Debentures (since exercised)
2022	Fairfax India	$65	$12/share
2022	Recipe	$346	Inreased ownership from 46 to 84%
2022	Grivalia	$195	Increased ownership from 33.5 to 78.4%
2022	Sporting Life		Increased ownership from 71 to 88.5%
	Total Consolidated	**$666**	

- Remaining Equity Holdings = $1.4 billion

These are the equity investments Fairfax does not exert a great deal of control over. They invested $1.4 billion the past three years. The biggest deal was expanding the partnership with Kennedy

Wilson in real estate, with the 2 transactions below being part of much the bigger deal (debt platform and PacWest loans). There are lots of 'solid single' type of investments on this list.

Fairfax - Investments in Non-Insurance - Other Equities			
June 2020 - June 2023		Amount	
Year	Holding	US$	Comments
2021	Helios Fairfax	$100	Debs and warrants
2022	Kennedy Wilson	$300	Preferred perpetual stock + 7 yr warrants
2022	Atlas	$78	Exercise warrants at $8.05/share
2022	Altius	$78	Exercise warrants at C$15/share
2022	Ensign	$9	Deb conversion at $C1.75/share
2022	John Keells	$75	208 mill debs
2022	Micron	$152	Add to position
2022	Foran Mining	$25	Exercise warrants at C$2.09/share
2022	Mytilineos	$53	Add to position at €18.50/share
2023	Atlas	$79	Exercise warrants (most at $13/share)
2023	Mytilineos	$53	Exchangeable bond €20/share
2023	Occidental	$130	Add to position
2023	Micron/BAC/Orla	$53	Add to position
2023	Kennedy Wilson	$200	Preferred stock + 7 year warrants ($16.21)
	Total Other	**$1,385**	

Summary

Over the past three years, Fairfax has invested a total of $6.2 billion to increase ownership in companies it already owns. Many of the investments were opportunistic and made at bear market low prices. Investments were made all over the world - value drove the decision, not geography. As a result, Fairfax (and its shareholders) now own a greater proportion of the future earnings streams of these many businesses. The returns on the investments made in recent years are starting to come in and they are very good (in aggregate). With lots of upside likely to come in the future.

Fairfax: Summary of Some of the Investments Made Over Last 3 Years	
Buying more of what they already own	
June 2020 - June 2023	**billion US$**
FFH Stock Buybacks	$1.535
FFH - TRS	$0.729
Insurance	$1.870
Non-insurance Equity Holdings	
Consolidated	$0.666
Other Equities	$1.385
Total Investments	**$6.185**

Conclusion: What did we learn?

How Fairfax is investing right now is incredibly simple. Invest in what you know. Buy at a discount. Act with conviction. Cast a wide net (global). Boring. Safe. Generating a very good return for shareholders. I think the masters would approve of what Fairfax has been doing. In short, Fairfax has been putting on a master-class in value investing over the past three years.

So, after all that, let's get back to our initial question.

What kind of an investor is Fairfax?

Fairfax is a value investor. Their approach is a hybrid of 5 masters: Lynch, Buffett, Graham, Templeton and Singleton.

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Some of the companies Fairfax owns a stake in are doing the same thing

The best example is Stelco, which has reduced shares count by 38% over the past 2.5 years. This has increased Fairfax's stake in the company from 14.7% to 23.6%.

Stelco	total			
	shares	30 month change		FFH %
Date	(millions)	shares	%	ownership
31-Dec-20	88.7			14.7%
30-Jun-23	55.1	-33.6	-38%	23.6%
Fairfax owns 13 million Stelco shares				

Actions like these provide additional benefits to Fairfax and its shareholders. When combined with what Fairfax is doing, they have a 'multiplicative' effect for Fairfax shareholders (in terms of owning a larger proportion of future earnings).

What Types of Investments Does Fairfax Make?

April 18, 2023

Fairfax is a value investor. One of the things that makes them unique compared to other insurance companies is the variety of platforms they are comfortable investing across in their search for value.

My goal with the list below is to try and capture the full range / types of investments Fairfax has made over the years. Successfully investing in each bucket requires a very different skill set. Yes, I probably have messed up with how some of the investments have been categorized. And some holdings could be included in more than one bucket.

Not included in the list below is the usual buy/sell large cap US/Canadian stocks as there are too many transactions to try and list everything that would fall into this bucket. With the list below, I am trying to highlight what Fairfax is doing in addition to this traditional strategy.

1.) <u>Venture capital investor</u>: funding given to start-ups or other young businesses that show potential for long-term growth:

- ICICI Lombard (1994) - sold for about $1.2 billion in 2017 and 2018. Home run.
- Quess - formerly IKYA (2013) - via Thomas Cook - still owns – solid investment.
- Digit (2016) – grand slam home run. IPO planned in 2024?
- Davos Brands, Rouge Media, Blue Ant Media (2016)
- Farmers Edge (2017) - a big miss
- Boat Rocker (2018)
- Ki (2020) – insurance via Brit

2.) <u>Venture debt investor</u>: using warrants as sweetener. Pre-2016, I think there were lots of these types of deals (too many to list).

- APR Energy and Chorus Aviation (2016)
- Mosaic Capital, Altius minerals, AGT Food and Ingredients, Westaim (2017)
- Seaspan (2018) - massive $500 million
- Leon's (2020)

3.) <u>Incubator/accelerator investor</u>: fostering early-stage companies through the different developmental phases (including funding to accelerate growth) until the companies have sufficient financial, human, and physical resources to function on their own.

- First Capital - Singapore (2002) - Sold for $1.7 billion in 2016.
- Riverstone UK - run-off (GFIC 2010) - Sold for @ $1.5 billion in 2020/21.
- Hartville Group (2013) & Pet Health (2014) - Sold for $1.4 billion in 2022.

4.) <u>Distressed/bankruptcy investor</u>: don't have the cash flow to service their debts and are fighting the clock:

- Bank of Ireland (2011) - Sold for more than $1.4 billion from 2014 to 2017.

- Eurobank (2014) – Bank has turned around and is now performing very well.
- Golf Town (2016) - Merged with Sporting Life.
- Performance Sports (2017) - Bauer/Easton/Cascade
- Carillion Canada/Dexterra (2018) - Merged with Horizon North in 2020.
- Toys "R" Us (2018) - Sold retail operations 2021. Now is a real estate play.

5.) Real estate investor

- Kennedy Wilson (2010) - Ongoing, growing and very successful partnership.
- Grivalia Properties - Greece (2011) - Very successful; merged with Eurobank in 2019.
- Grivalia Hospitality (2022)

6.) Asset manager

- Fairfax India (2015) - Ownership has increase from 28% to 42%.
- Fairfax Africa (2017) - Merged with Helios in 2020 - spectacular failure.

7.) Private equity investor (via external fund managers) - funds allocated here continue to meaningfully grow:

- BDT Capital (since 2009)
- ShawKwei
- JAB JCP V investment fund (2022)
- Lots more

8.) Turnaround investor: not fighting the clock. Many of Fairfax's investments became 'turnaround' situations after Fairfax made their initial investment especially 2015-2017 vintage.

- Sandridge Energy (2008/09) – Entered bankruptcy in 2016?
- Abitibi/Resolute (2008) – Resolute was sold in 2022 for $626 million plus $183 million CVR
- The Brick - Merged with Leon's 2012. Leon's position was sold in 2021 for $140 million.
- Blackberry (2011) – looking more and more like a spectacular failure.
- Torstar - Sold in 2020.
- Reitmans (2013) - Sold in 2019.
- EXCO Resources - Bankruptcy - take private 2019 (Fairfax owns 44%).
- Fairfax Africa (2015) - Merged with Helios in 2020.
- APR (2016) - Sold to Seaspan/Atlas in 2019.
- AGT Food Ingredients (2017) - Take private in 2019.
- Mosaic Capital (2017) - Take private in 2021 (not managed by Fairfax).

9.) Commodity investor

- International Coal Group (2006-09) - Coal play - sold for big gains.
- Sandridge Energy (2008/09) – Entered bankruptcy in 2016?
- Abitibi/SFK Pulp/Resolute (2006-09) - Paper, pulp & later lumber. Sold in 2022.
- Tembec (2015) - lumber - Sold in 2017.
- EXCO Resources - natural gas - Bankruptcy/take private 2019.
- Altius Resources (2017) - Resource royalty play.

- Ensign Energy Services (2018) - Oil and gas services.
- Stelco (2018) - Steel producer.
- Foran Mining (2021) – Early stage copper play.

10.) International investor (2014 was a big year)

- Bank of Ireland (2011)
- Grivalia (2011)
- Mytileneos (2013)
- Eurobank (2014)
- Thomas Cook (2014)
- CIB Bank (2014)
- IIFL
- John Keells

11.) Cannibal investor: opportunistically increasing ownership in businesses it already owns a part of. Low risk / high return.

- 1.95 million shares in Fairfax (TRS) at $373/share.
- 2 million shares in Fairfax (stock buyback) at $500/share.
- Increased ownership in Allied World from 70.9% to 82.9% for $733 million.
- Increase stake in Recipe to 84% for $346 million ($100 million from Recipe).
- Increase stake in Grivalia Hosiptality from 33.5% to 78.4% for $195 million.
- Kennedy Wilson preferred equity = $300 million.
- Increase stake in Eurolife from 50% to 80% for $143 million.
- Increase stake in Singapore Re from 28.1% to 100% for $103 million.
- Ownership in Atlas was also increased over this time-frame.
- Fairfax spent another $300 million increasing their ownership in the following companies: Fairfax India, John Keells, Mytilineos, Foran Mining, Altius and Ensign Energy.

Capital Return

When looking at capital deployment in general, Fairfax's top priority since the start of the hard market in late 2019 has been to support organic growth of the insurance operating companies.

In terms of capital return, Fairfax has been very active in recent years on the share buyback front and it also pays a modest dividend. We review both of these items below.

Share Buyback History

Updated February 19, 2024

The big picture

Three factors drive stock returns over the long term:

- earnings
- multiple
- shares outstanding

The last factor is often ignored by investors.

Capital allocation

Capital allocation is the most important function of a management team and stock buybacks are one of many options that are available.

Share buybacks can be very beneficial for shareholders if they are done in a responsible manner (purchased at attractive prices) and sustained over many years.

It is counterintuitive, but for long term shareholders a low share price can be a big benefit - if the company is buying back shares and in a significant quantity. Especially if it persists for years.

How does Fairfax approach buybacks?

Prem laid out Fairfax's strategy regarding share buybacks in the 2018 annual report:

> "I mentioned to you last year that we are focused on buying back our shares over the next ten years as and when we get the opportunity to do so at attractive prices. Henry Singleton from Teledyne was our hero as he reduced shares outstanding from approximately 88 million to 12 million over about 15 years." *Prem Watsa – Fairfax 2018AR*

Fairfax approaches share buybacks from the framework of a value investor: buy back shares when they are cheap and back up the truck when they are really cheap.

What has Fairfax been doing in recent years?

Fairfax's year-end 'effective shares outstanding' peaked in 2017 at 27.75 million. Fairfax issued a total of 7.2 million shares in 2015, 2016 and 2017 to help fund its aggressive international expansion in insurance. The new shares were issued at an average price of about $462/share.

At December 31, 2024, the 'effective shares outstanding' at Fairfax had fallen to 23.0 million shares. Over the last 6 years (2017-2023), Fairfax has reduced its share count by approximately 4.75 million shares or 17.4%. The average price paid to buy back shares was about $484/share.

The average price paid for the shares repurchased by Fairfax over the past 6 years is slightly higher than the price that shares were issued at from 2015-2017. Fairfax's book value at December 31, 2023 was $940/share. Fairfax has been able to buy back a significant number of shares at a very attractive average price – more than 50% below book value, which is below intrinsic value.

The big share re-purchase was in December 2021, when Fairfax executed a Dutch auction and purchased 2 million shares at US$500/share at a total cost of $1 billion. To fund the purchase, Fairfax sold 10% of Odyssey for US$900 million. The management team at Fairfax was both creative and opportunistic in executing this transaction.

Over the past 6 years, Fairfax has done an outstanding job of buying a significant number of shares at prices well below book value. This is just another demonstration of the outstanding job the management team at Fairfax has done when it comes to capital allocation.

Fairfax - Total Reduction In Share Count Last 6 Years

US$ Date	Effective Shares Outstanding million	Share Reduction million	Avg Cost Per Share	Total Cost billion $
2017	27.8			
2018	27.2	0.51	$509	$0.262
2019	26.8	0.41	$464	$0.188
2020	26.2	0.66	$298	$0.195
2021	23.9	2.31	$490	$1.132
2022	23.3	0.54	$509	$0.275
2023	23.0	0.32	$764	$0.246
Total	**17.4%**	**4.75**	**$484**	**$2.298**
6-YR AVG	2.9%			

Fairfax’s total return swaps (TRS) on 1.96 million Fairfax shares

Some investors consider this investment to represent a buyback of sorts. Here is an update on this holding. It is turning into one of Fairfax’s best investments ever.

The TRS-FFH has increased in value by about $1.27 billion, or more than 174% over 38 months (not including the costs to maintain the position).

Fairfax		**FFH**	**TRS**	**TRS cumulative**		
Total Return Swaps		**share**	**market**	**increase in value**		
1.96	mill share	**price**	**value**	**$**	**%**	**per share**
Late 2020/Early 2021		$373	$731	Value at at inception		
Feb 16, 2024		$1,022	$2,003	$1,272	174%	$55

What does Warren Buffett have to say about share buybacks?

“A very minor gain in per-share intrinsic value took place in 2022 through Berkshire share repurchases as well as similar moves at Apple and American Express, both significant investees of ours. At Berkshire, we directly increased your interest in our unique collection of businesses by repurchasing 1.2% of the company’s outstanding shares. At Apple and Amex, repurchases increased Berkshire’s ownership a bit without any cost to us.

“The math isn’t complicated: When the share count goes down, your interest in our many businesses goes up. Every small bit helps if repurchases are made at value-accretive prices. Just as surely, when a company overpays for repurchases, the continuing shareholders lose. At such times, gains flow only to the selling shareholders and to the friendly, but expensive, investment banker who recommended the foolish purchases.

“Gains from value-accretive repurchases, it should be emphasized, benefit all owners – in every respect. Imagine, if you will, three fully-informed shareholders of a local auto dealership, one of whom manages the business. Imagine, further, that one of the passive owners wishes to sell his interest back to the company at a price attractive to the two continuing shareholders. When completed, has this transaction harmed anyone? Is the manager somehow favored over the continuing passive owners? Has the public been hurt?

“When you are told that all repurchases are harmful to shareholders or to the country, or particularly beneficial to CEOs, you are listening to either an economic illiterate or a silver-tongued demagogue (characters that are not mutually exclusive).”

Warren Buffett - Berkshire Hathaway 2022AR

Dividend History

Update: Jan 3, 2024

Fairfax increased its dividend from US$10 to US$15/share, payable Jan 25.

"Given Fairfax's substantial growth since it inaugurated a US$10 per share annual dividend 14 years ago, and given Fairfax's current position of foreseeing strong earnings for the next few years based on insurance company underwriting income, locked-in interest and dividend income and income from associates, we felt it was appropriate to raise our annual dividend this year to US$15 per share, and we believe that this should be a sustainable level," said Prem Watsa, Chairman and Chief Executive Officer of Fairfax. *Fairfax Press Release Jan 3, 2024*

October 12, 2023

Like many other P/C insurers, Fairfax pays a modest dividend:

- US$10/share = 1.2% yield (based off the closing price of the stock today of $832).
- Paid in one annual instalment in January of each year.
- Paid continuously since 2001, when it started at C$1.00/share.
- The current amount of $10/share has been paid since January 2011.

Moving forward, it is likely Fairfax will continue to pay a dividend of at least $10/share.

- Is the dividend secure? Yes – based on the level of Fairfax's earnings.
- When will the dividend be increased? Perhaps once Fairfax has bought out their minority partners in Odyssey and Allied (2025?).

Below are a couple of interesting quotes from past annual reports.

<u>2022 Annual Report</u>

"As expected, we maintained our dividend of $10 per share in 2022 and used our excess cash flow to buy back 387,790 shares in the market. Since we began paying cash dividends, we have paid cumulative dividends of $3.4 billion or $152 per share. Our book value per share would have been $152 per share or 23% higher if we had retained all our earnings. Don't forget the dividends in your return calculation!" *Prem Watsa - Fairfax 2022AR*

Prem reminds investors to include dividends when they calculate total returns.

In 2011, the dividend was increased significantly to $10/share.

> "Given our results for 2010, our significant holding company cash and marketable securities position, the availability to us of the free cash flow of our insurance and reinsurance companies now that our largest companies are 100% owned, and our strong and conservative balance sheet, in early 2011 we paid a dividend of $10 per share (an extra $8 per share in excess of our nominal $2 per share). The amount above the nominal amount for any year will reflect the prevailing circumstances." *Prem Watsa Fairfax - 2010AR*

In 2000, the dividend was initiated – at the same time Prem's salary was fixed at C$600,000/year.

> "This brings me to my own compensation arrangements. For many years now I have felt that as a controlling shareholder involved in the management of the company, my compensation should be closely linked to all shareholders. So from 2000 onwards, my compensation will be a fixed salary of $600,000 with no bonuses. This compensation will not increase annually, and if 1999/2000 is repeated, could decrease!! However, to make sure that my family survives, Fairfax will examine instituting a dividend – yes, a modest dividend – in 2001 at an annual rate of $1 or $2 per share. Going forward, the only difference between me and you, our shareholders, will be my salary of $600,000 – which based on recent performance, many of you may think is too high! While the payment of a modest dividend results in double taxation to most of you and is not as economically efficient as retaining all our profits and compounding at high rates of return (as we have done for the past 15 years), this was the only way I could think of to bring my compensation in line with your interests." *Prem Watsa – Fairfax 2000AR*

Chapter 6: Insurance

Insurance: The Diamond in the Rough

April 16, 2023

While the equity portfolio at Fairfax gets most of the attention, the real jewel at Fairfax is the insurance business. It has grown in size by 420% since the end of 2009 (both organically and by acquisition). Net premiums written increased from $4.3 billion in 2009 to $22.3 billion in 2022. Fairfax has demonstrated they are excellent at seeding new insurance companies/management teams and then getting out of the way. They are also good at making and integrating acquisitions.

Andy Barnard was put into his role in 2011 - managing the insurance side of Fairfax. He manages the business through 200 profit centres, which indicates just how decentralized the insurance operations are. Fairfax has insurance companies all over the world that are quietly growing year after year. Lots of the value has likely been building in this group for decades and is NOT captured in book value. For people who need convincing see the list below.

Over the past 6 years Fairfax has opportunistically monetized a few of their insurance businesses and this has resulted in pre-tax gains of more than $4 billion. Yes, Digit, seeded in 2017, has become a home run. Ki, seeded in 2020, is growing rapidly. Gulf Insurance Group, seeded in 2010, has quietly grown into a very large insurance company in the MENA region. Lots of good things are happening under the hood at the insurance businesses at Fairfax.

<u>Sales of Insurance Businesses:</u>

1. First Capital - Singapore
    - Seeded in 2002 and sold in 2017 for a $1.02 billion after-tax gain.
    - Delivered a compound rate of return of 30% since 2002.

2. ICICI Lombard - India
    - Seeded in 2001.
    - Sold in 2017 (down to 10%) and remainder in 2019 for about a $950 million pre-tax gain.
    - Fairfax had to sell ICICI Lombard (down to 10%) to invest in Digit.

3. Riverstone Europe - runoff
    - Sold in 2020 & 2021 for proceeds of $1.3 billion (plus $230 million contingent value instrument).

4. Pet Insurance
    - Seeded with two purchases in 2013 and 2014.
    - Sold in 2022 for a $992 million after tax gain.

5. Ambridge Partners
    - Purchased by Brit in two transactions in 2015 and 2019.
    - Sold in 2023 for $255 million pre-tax gain.

Allied World

October 12, 2023

With underwriting profit of $389 million, the top performing insurance sub at Fairfax in 2022 was Allied World. Fairfax purchased Allied World back in 2017 for $4.9 billion (at 1.3 x book value). Fairfax made a number of acquisitions in 2015 (Brit), 2016 (international) and 2017 (Allied). Of all the purchases, Allied was, by far, the largest.

To help fund the purchase of Allied, Fairfax partnered with OMERS, AimCo and 2 other investors.

What was the funding split? Fairfax = 67.4% and OMERS/AimCo/others = 32.6%

To help fund its purchase of Allied World in 2017, Fairfax also issued a little over 5 million shares at $433/share. From 2018 to 2022, Fairfax repurchased 4.4 million shares at an average cost of $464/share. Fairfax has been very opportunistic in recent years buying back shares at very attractive prices. As a result, the significant dilution caused by the Allied World acquisition has almost been entirely reversed. And Fairfax now owns a larger stake in a company that has more than doubled in size over the past 5 years.

The acquisition of Allied World in 2017 was very opportunistic: the company was purchased at 1.3 x book value and right before the onset of a hard market (which began in late 2019 and continues in 2023). Bringing in minority partners to help fund the purchase was very creative. I must admit I still do not understand all the puts and takes of the deal with OMERS/AimCo - the deal carries a high cost (8% dividend?) but allows Fairfax the ability to increase its ownership when it has the cash.

Over the past 6 years Fairfax has purchased about 50% of the minority interest held in Allied. Today, Fairfax owns 83.4% of Allied and minority shareholders own 16.6% (down from 32.6%).
- In 2022, Fairfax's largest 'investment' was the $733 million spent to increase its ownership in Allied from 70.9% to 82.9%.
- In Q2 2023, Fairfax spent $30.6 million to increase their ownership of Allied to 83.4%.

Fairfax has the option to purchase the remainder of Allied World from the minority partners until September of 2026 (this option was extended by 2 years in Q2, 2023).

Increasing its ownership in Allied World is a solid move for Fairfax shareholders as they will own a larger percentage of Allied World's growing earnings. Some on this board have stated Fairfax buying out minority shareholders is similar to buying back shares of its own stock. It is a low risk and solid return use of capital for Fairfax.

How much would Allied World be worth today as a stand-alone company?

- Net written premiums (2023 est) = $4.9 billion
    - Estimated underwriting profit at a 95% CR = $245 million
- Investment portfolio (Dec 31, 2022) was $11.5 billion
    - Estimated total investment return at 6% = $690 million

Interesting factoid: The purchase of Allied World did not start out well. The deal closed in July of 2017. Then 3 major hurricanes hit the US. In the 2H-2017, Allied World booked a $600 million pre-tax loss at Fairfax. Ouch!

Link to video: Overview of Allied World (from company's web site)

https://alliedworldinsurance.com/wp-content/uploads/sites/2/2023/01/Our-Culture-2023.mp4

Prem's comments about Allied World from Fairfax's 2022AR.

"Allied World produced $389 million of underwriting profit in 2022 from a combined ratio of 91%, also its best performance as a Fairfax company. After growing net premiums written 14% last year, Allied is now double in size from when we purchased it in 2017. Allied's expense ratio continued to decline in 2022, now running at an industry leading 20%. Lou Iglesias and his management team have done an outstanding job aggressively expanding over the last several years in the market segments which experienced the strongest growth." *Prem Watsa – Fairfax 2022AR*

The table below shows our growth since 2017, after we had purchased Allied World and in the midst of a hard market in insurance that began in 2019:

	Gross Premiums Written			Average
	2017	2022	% change	Combined Ratio
	($ billions)			
Northbridge	1.2	2.3	95%	92%
Odyssey Group	2.7	6.6	141%	96%
Crum & Forster	2.1	4.6	116%	97%
Brit	2.0	4.0	93%	102%
Allied World	3.1	6.5	110%	94%
Total	13.8	27.6	99%	96%

The table below shows you how our significant increases in gross premiums written have resulted in a significant increase in our float and in our investment portfolio. This is magnified on a per share basis as a result of the reduction in our outstanding shares through share buybacks which have reduced our shares outstanding by 16% over the last five years, from 27.8 million at the end of 2017 to 23.3 million at the end of 2022:

In the 2022AR, Fairfax explains the accounting mechanics of the take-out of minority partners.

"On September 27, 2022 the company increased its ownership interest in Allied World to 82.9% from 70.9% for total consideration of $733.5, inclusive of the fair value of a call option exercised and an accrued dividend paid, and recorded a loss in retained earnings of $228.1 in net changes in capitalization in the consolidated statement of changes in equity. The decrease in carrying value of Allied World's non-controlling interests primarily reflected the company's increased ownership interest in Allied World, dividends paid and the non-controlling interests' share of Allied World's net loss. On April 28, 2022 Allied World paid a dividend of $126.4 (April 28, 2021 – $126.4) to its minority shareholders. The company has the option to purchase the remaining interests of the minority shareholders in Allied World at certain dates until September 2024." *Fairfax 2022AR*

Summary of the key details regarding the acquisition of Allied World from Fairfax's 2017AR.

"Acquisition of Allied World Assurance Holdings AG: On July 6, 2017 the company completed the acquisition of 94.6% of the outstanding shares of Allied World Assurance Company Holdings, AG ("Allied World AG") for purchase consideration of $3,977.9, consisting of $1,905.6 in cash and $2,072.3 by the issuance of 4,799,497 subordinate voting shares. In addition, Allied World AG declared a special pre-closing cash dividend of $5.00 per share ($438.0). Contemporaneously with the closing of the acquisition of Allied World AG, Ontario Municipal Employees Retirement System ("OMERS"), the pension plan manager for government employees in the province of Ontario, Alberta Investment Management Corporation ("AIMCo"), an investment manager for pension, endowment and government funds in the province of Alberta, and certain other third parties (together "the co-investors") invested $1,580.0 for an indirect equity interest in Allied World AG. The remaining 5.4% of the outstanding shares of Allied World AG were acquired on August 17, 2017 for purchase consideration of $229.0, consisting of $109.7 in cash and $119.3 by the issuance of 276,397 subordinate voting shares, in a merger transaction under Swiss law pursuant to which Allied World Assurance Company Holdings, GmbH ("Allied World") became the surviving entity. This merger resulted in the co-investors holding an indirect ownership interest in Allied World of 32.6%. The co-investors will have a dividend in priority to the company, and the company will have the ability to purchase the shares owned by the co-investors over the next seven years. Allied World is a global property, casualty and specialty insurer and reinsurer."

"As you can see, while this acquisition increased our gross premiums, investment portfolio and common equity by about 30%, our shares outstanding grew by only 22%. Although we issued the Fairfax shares at a 6% premium to book value while we purchased Allied World at a 32% premium to book value, we are confident that the high quality of Allied World, let by Scott Carmilani, will make this an excellent acquisition for us, but we were not pleased at issuing our shares at only a 6% premium to book value." *Fairfax 2017AR*

We closed our acquisition of Allied World on July 6, 2017 and we welcomed Scott Carmilani and Allied World's 1,430 employees to the Fairfax family. As you know, Allied World is the largest acquisition that we have done and we pursued this acquisition because of Allied World's outstanding track record over its 15 years of existence and the quality of its management team. We are very thankful to our financing partners OMERS ($1 billion), AIMCO ($0.5 billion) and two others. We issued a total of 5.1 million shares for Allied World. The effect of this acquisition is shown in the table below, which was previously presented to you at our 2017 annual shareholders' meeting:

($ billions)	**Fairfax**	**Allied World**	**Combined**	**% Change**
Gross premiums written	10.2	3.1	13.3	30%
Investment portfolio	27.4	8.7	35.3(1)	29%
Common shareholders' equity	8.5	3.6	10.9(1)	28%
Shares outstanding *(millions)*	23.1		28.2	22%
Investments per share *($)*	1,186		1,250	5%

(1) Combined numbers adjusted for financing and goodwill

In May 2023, AM Best upgraded the credit ratings of Allied World.

AM Best Upgrades Issuer Credit Ratings of Fairfax Financial Holdings Limited, Its Subsidiaries and Allied World Assurance Company Holdings, Ltd.

"Furthermore, AM Best notes that Allied World's **operating performance has been on a steadily positive trajectory for the last five years**, reflecting broad rate improvement across many of the company's key business lines, as well as **changes in underwriting strategy**. Notably, the company has **reduced its catastrophe exposure, which has reduced volatility**. AM Best expects that Allied World's risk-adjusted capitalization as measured by the Best's Capital Adequacy Ratio (BCAR) will continue to be supportive of the overall balance sheet assessment, supported by capital growth from operating earnings and supplemented by an eventual recovery of equity and fixed income markets prices over time.

https://www.businesswire.com/news/home/20230503005889/en/AM-Best-Upgrades-Issuer-Credit-Ratings-of-Fairfax-Financial-Holdings-Limited-Its-Subsidiaries-and-Allied-World-Assurance-Company-Holdings-Ltd

Digit

March 1, 2024

India regulator clears Fairfax-backed Digit's IPO after delay, letter shows

https://www.reuters.com/world/india/india-regulator-clears-fairfax-backed-digits-ipo-after-delay-letter-shows-2024-03-01/

July 31, 2023

Digit has become one of Fairfax's best investments ever. And it has the potential to become THE best investment ever. Yes, I know, big words. If that is the case, then why is the write up on Digit so short? Digit is a great example of one of the big shortcomings with this document - it is missing a lot of important information. The reader needs to keep this in mind.

For a little more information on Digit go to 'Chapter 12: Geographies' and read the post on India.

How much of Digit does Fairfax own?

- Currently 49%
- This will increase to 74% 'upon conversion of securities, one regulatory approval is received' The quote is from the 2022AR.

How has Fairfax's investment in Digit performed?

Fairfax's investment in Digit has a total cost of $154 million. Fair value at December 31, 2023 is 2.278 million. Fairfax's investment in Digit is up $2.1 billion for a compound annual return of 79.5%. Spectacular. The table below is from the 2022AR.

The table below shows our investments in India and how they have performed up to December 31, 2022:

	Date of Initial Investment	Ownership	Cost	Fair Value at December 31, 2022	Compound Annualized Return
Thomas Cook India	Aug-12	73.3%	315	293	10.7%(1)
Fairfax India	Jan-15	41.6%	534	703	4.3%
Digit	Feb-17	49.0%	154	2,278	79.5%
Quess	Dec-19	30.1%	335(2)	222	(7.1)%
Other			365	308	
			1,703	3,804	

Prem's comments about Digit from Fairfax's 2022AR.

"Digit, led by Kamesh Goyal, had another strong year: after only five years since its inception, premiums are over $900 million, up 50% over the last 12 months in local currency, and with the benefit of investment income it had another profitable year. Digit entered the Fortune India magazine's ranking of India's 500 largest companies by total revenue during the year at 398th on the list – we expect that will move up going forward! Digit is exploring an IPO in 2023 which would fund future growth." *Prem Watsa – Fairfax 2022AR*

Prem's comments about Digit from Fairfax's 2021AR.

"Digit, under Kamesh Goyal, continued its exceptional performance in 2021 as a start-up (five years ago), with gross premiums expected to be up 50% to $700 million for the year ending March 2022. Recently, Kamesh raised $200 million, valuing Digit at $3.5 billion – the first unicorn in India in 2021. Unlike many unicorns, Digit is already profitable. As you will see later, this capital raise, including Sequoia (awaiting regulatory approval) and Wellington among its investors, contributed $1.5 billion to our net gains in 2021. More to come we think!" *Prem Watsa – Fairfax 2021AR*

Gulf Insurance Group

Updated: December 14, 2023

KIPCO announced the closing of the sale of their 46.3% interest in the Gulf Insurance Group (GIG) to Fairfax. Fairfax's equity interest in GIG increased from 43.7% to a controlling interest of 90.0%.

KIPCO completes the sale of its 46% stake in GIG to Fairfax Financial Holdings

https://kipco.com/kipco-completes-the-sale-of-its-46-stake-in-gig-to-fairfax-financial-holdings/

Based on the financial details that were provided in Fairfax's Q3 interim report, Fairfax is making an upfront payment of around $177 million. And then 4 equal annual payments of $165 million, beginning Dec 14, 2024.

"The company's acquisition of all of KIPCO's shares in Gulf Insurance will be for aggregate fair valuation consideration of approximately $740 (approximately 227 million Kuwaiti Dinar), to be paid as approximately $177 in cash ($200.0 less dividends of approximately $23 received by KIPCO during the second quarter of 2023) and the fair value of approximately $563 in a payment deed."

Fairfax Q3 Interim Report

Fairfax will book a significant gain of around $290 million when it reports Q4 results.

> "Accordingly, the company anticipates that upon closing it will consolidate the assets and liabilities of Gulf Insurance and will record a pre-tax gain of approximately $290, with changes in the company's carrying value of its equity accounted investment in Gulf Insurance up until the date of closing affecting the pre-tax gain." *Fairfax Q3 Interim Report*

The structure of the deal is very creative – it appears a large part of the 4 equal annual payments of $165 million could be funded each year via dividend payments from GIG to Fairfax.

> "We structured it (the deal) in a way that perhaps a lot of it (annual payments) will come from the company itself, dividends from the company." *Prem – Fairfax Q1, 2023 Conference Call*

This purchase will be an important growth driver for Fairfax's results in 2024. The timing of the news is important (before year-end), so we will get more complete details of the financial impact on Fairfax when they report Q4 results in Feb 2024. Now that the deal has closed, analysts can include GIG in their estimates for Fairfax for 2024.

<u>Below are highlights of GIG's full year financial results from 2022</u>:

- Net premiums written $1.7 billion
- Underwriting surplus $164 million
- Total Investments $2.4 billion
- Shareholder's equity $748 milion
- Net profit $125 million

<u>Some random thoughts on the GIG purchase</u>:

- Fairfax goes from being a minority shareholder in GIG to the controlling shareholder. This is a big deal.
- Strategically, this secures Fairfax's position as one of the leading P/C insurance providers in the Middle East North Africa (MENA) region. This is a big deal. Gulf economies, with young and growing populations, are expected to be strong growers in the coming decade. Growing economies should be good for an insurance business.

This purchase highlights a couple of strengths of Fairfax:

- International - this has been a growing part of Fairfax's insurance business for 20 years
- Partner with leading organizations - in this case KIPCO
- Long term focus - this transaction was incubating for 13 years

<u>Capital allocation</u>

Fairfax is earning a record amount of operating earnings in 2023 and the set-up for the next couple of years looks very promising. What will Fairfax do with all the cash that is raining down?

“The best stock to buy is the one you already own.” *Peter Lynch*

The past couple of years, Fairfax has been cannibal investing (gorging) - buying significantly more of companies it already owns. GIG is the latest example of this strategy. Fairfax owned 43.7% and now they own 90%.

This is such a good strategy because it is very low risk. They understand GIG very well, having been closely involved with the company for the past 13 years. Fairfax is also paying up for quality (and to get control of the company).

Bottom line, this purchase makes Fairfax a more profitable and higher quality company.

GIG updated their web site in 2024 with lots of new information. Below are links to a couple of presentations and investor relations.

Investor Presentation – May 2023 (short – 7 pages)

https://www.gulfinsgroup.com/media/GIG_Investor_Presentation_2023_EN_Final.pdf

Corporate Profile

https://www.gulfinsgroup.com/media/GIG-Corporate-Profile-ENG_D5wymRk.pdf

Investor Relations

https://www.gulfinsgroup.com/en/investor-relations/

In 2010, Fairfax invested $217 million for a 41.3% interest in Gulf Insurance. Fairfax partnered with KIPCO (Kuwait), the controlling shareholder of Gulf Insurance.

GIG became the vehicle for Fairfax to grow its insurance business in the MENA region (Middle East North Africa). The growth for the next 10 years was largely organic.

Late in 2020, as the world was struggling with covid, GIG opportunistically agreed to purchase the insurance operations of AXA Gulf & Yusuf Bin Ahmed Kanoo for $475 million. This purchase almost doubled the size of GIG - it was a big, bold move. Parent AXA was looking to re-build its capital levels due to losses experienced from covid. The purchase closed in Sept of 2021. Fairfax did invest new money in GIG (as did KIPCO) in 2021 to keep its ownership in GIG steady at 43.7% (not sure exactly how much they spent).

The shares of GIG are publicly traded on the Kuwait stock exchange. However, they are thinly traded, with KIPCO and Fairfax together owning 90%.

Who is KIPCO?

Kuwait Projects Company (Holding) – KIPCO – is a holding company that focuses on investments in the Middle East and North Africa. It's strategy of acquiring, building, scaling and selling companies in the MENA region has worked successfully for over 30 years.

https://kipco.com

Historical Information

Gulf Insurance Group

billions	Gross Premiums	CR	Investment Portfolio
2022	$2.676	92	$2.407
2021	$1.818	94	$2.422
2020	$1.449	93	$0.991
2019	$1.297	95	
2010	$0.418		$0.552

millions	Own %	Fair Value	Carrying Value	Share of Profit
2022	43.7%	$415.8	$403.4	$53.0
2021	43.7%	$409.5	$380.0	$55.5
2020	43.4%			$5.8
2019	43.6%			$15.4
2010	41.3%	$219.9	$219.9	

From Fairfax's Q3 Interim Report

Subsequent to September 30, 2023 *Acquisition of additional interest in Gulf Insurance*
"On April 19, 2023 the company entered into an agreement to acquire all shares of Gulf Insurance under the control of KIPCO and certain of its affiliates, representing 46.3% of the equity of GIG. In accordance with applicable Kuwaiti regulatory requirements and the rules of the Boursa Kuwait, the exchange on which Gulf Insurance's shares are traded, the company will pay the purchase price to KIPCO in full in Kuwaiti Dinar on closing. Pursuant to the terms of the agreement, immediately following settlement of the transaction, KIPCO shall return to the company in cash the full purchase price less an amount of Kuwaiti Dinar equal to $200.0, together with a cash payment equal to all dividends received by KIPCO from Gulf Insurance after Jan 1, 2023, and the company will deliver to KIPCO a payment deed of $660.0 which requires the company to make four equal annual payments of $165.0 to KIPCO beginning on the first anniversary of closing of the transaction.

"The company's acquisition of all of KIPCO's shares in Gulf Insurance will be for aggregate fair valuation consideration of approximately $740 (approximately 227 million Kuwaiti Dinar), to be paid as approximately $177 in cash ($200.0 less dividends of approximately $23 received by KIPCO during the second quarter of 2023) and the fair value of approximately $563 in a payment deed. Closing of the transaction is subject to customary closing conditions, including regulatory approvals, and is expected to be in the fourth quarter of 2023. On closing of the transaction, the company's equity interest in Gulf Insurance will increase from 43.7% to a controlling interest of 90.0%. Accordingly, the company anticipates that upon closing it will consolidate the assets and liabilities of Gulf Insurance and will record a pre-tax gain of approximately $290, with changes in the company's carrying value of its equity accounted investment in Gulf Insurance up until the date of closing affecting the pre-tax gain." *Fairfax's Q3 Interim Report*

Prem's comments about GIG from Fairfax's 2022AR.

"Gulf Insurance Group had another excellent year led by CEO Khaled Saoud Al-Hasan and GIG Gulf CEO Paul Adamson. 2022, the first full year with GIG Gulf results, produced gross premiums of over $2.5 billion and a combined ratio of approximately 92%. We have a wonderful partnership with Kipco, led by CEO Sheikha Dana, in the ownership of Gulf Insurance."

"Bijan (Khosrowshahi), along with Jean Cloutier, have been deeply involved with Gulf Insurance Group in the Middle East as well. After the acquisition of AXA Gulf (now GIG Gulf) in 2021, Gulf Insurance is one of the most prominent players in the region. Led by Khaled Al-Hasan, with Paul Adamson running GIG Gulf as a standalone unit, Gulf Insurance will be an increasingly important contributor to Fairfax." *Prem Watsa – Fairfax 2022AR*

Prem's comments about GIG from Fairfax's 2021AR.

"I mentioned this to you in last year's annual report but it bears repeating. We have had a wonderful partnership with Kipco in the ownership of Gulf Insurance Group (GIG) in Kuwait. GIG is run by Khaled Saoud Al- Hasan, until just recently under the chairmanship of Faisal Al-Ayyar, the CEO of Kipco. GIG had $1.8 billion (including four months of AXA Gulf) in premiums in 2021, more than 3 times the premiums in 2010 when we became a partner (our interest is 44%). Khaled has an outstanding track record with an average combined ratio of 95%, with excellent reserving. As mentioned last year, GIG acquired AXA Gulf (now GIG Gulf) on September 7, 2021, which had $1 billion in premiums in 2021 and a combined ratio of 93%. The new GIG, operating in 13 countries with $2.6 billion in gross premiums, will be a force to be reckoned with. Paul Adamson and his team have done an outstanding job at AXA Gulf. From Fairfax, Bijan Khosrowshahi, Jean Cloutier and Quinn McLean have been very involved in the success of our partnership with GIG. It is with great regret that I have to announce that our partner, Faisal Al-Ayyar, has recently retired after a stellar 30+ year career with Kipco. He has been a wonderful friend and partner to Fairfax and myself and we will miss him greatly. We wish Faisal and his family much happiness and good health in his retirement. Sheikha Dana is the new CEO of Kipco and our partner at GIG. We look forward to working with her in the years to come." *Prem Watsa – Fairfax 2021AR*

Investing activities for the year ended December 31, 2021

"Purchases of investments in associates of $175.4 primarily related to increased investments in Gulf Insurance, HFP and a Fairfax India associate."

Prem's comments about GIG from Fairfax's 2010AR.

"Gulf Insurance consolidates our interests in the Middle East."

"In 2008 we mentioned to you that we had purchased approximately a 20% interest in Arab Orient run excellently by Isam Abdelkhaliq and controlled by Karim Kabariti (Chairman of Jordan Kuwait Bank). Through Karim we met Faisal Al Ayyar, Vice Chairman of Kipco, the controlling shareholder of Gulf Insurance and Jordan Kuwait Bank and the ultimate controller of Arab Orient. Under Faisal's leadership, Kipco has had an outstanding track record over the past 20 years, increasing shareholder value by building businesses with an Arab world focus. Kipco's book value per share has compounded by 16% per year over the past 13 years and the stock price has followed suit. We paid $217.1 million for a 41% interest in Gulf Insurance, with Kipco having a 43% interest, and Gulf Insurance purchased our shares of Arab Orient at our cost of $11.2 million to increase Gulf's ownership of Arab Orient to 89%. Gulf Insurance, which has been in business since 1962, operates in seven countries in the Middle East and North Africa and is the premier property and casualty company in the region. In 2010, Gulf Insurance wrote $417.6 million in gross premiums and earned $33.2 million, with a consolidated investment portfolio of $552.0 million; its combined ratio has averaged 94% over the past ten years. We are excited to be partners with Faisal and his management team at Kipco and our team of Bijan Khosrowshahi, Jean Cloutier and Steve Ridgeway look forward to working with Khaled Saoud Al-Hasan, the CEO of Gulf Insurance, and the presidents of the seven insurance companies belonging to Gulf Insurance. We continue to separately own a 20% interest in Alliance Insurance Company in Dubai, led by Wisam Al Haimus. Wisam had another outstanding year with a combined ratio of approximately 74% in 2010." *Fairfax 2010AR*

Press release from 2020 with details of GIG's acquisition of AXA Gulf/Yusuf Bin Ahmed Kanoo.

"Gulf Insurance Group CEO Khaled Saud Al-Hassan said in an interview with "Al Arabiya" today, Tuesday, that the acquisition of the entire stake in "AXA Gulf" by Gulf Insurance is part of the group's strategy to increase revenue and its presence in the Arab region.

"He added that Gulf Insurance is currently present in 11 countries and its revenues totaled $ 1.5 billion in 2020, and the acquisition is part of the board's policy for regional expansion and leadership in Arab insurance markets. operations and net profit.

"Gulf Insurance Group CEO explained that Gulf Insurance Group is present in countries including Egypt, Algeria and Turkey, as well as other Arab markets, and these countries account for 50% of the group's total revenues and Kuwait accounts for the remaining percentage.

"Khaled Saud Al-Hassan indicated that the acquisition of AXA Gulf will increase the group's revenues to $ 2.5 billion, making it the largest player in the Arab insurance market and is present in 13 countries, adding Qatar, Oman and Abu Dhabi after the acquisition, in in order to serve customers and shareholders."

https://asumetech.com/gulf-insurance-in-al-arabiya-the-acquisition-of-axa-brings-revenues-to-2-5-billion-dollars/

Odyssey Group – Link to Enduring Momentum Book (2021)

In 2021, the Odyssey Group published a book, called Enduring Momentum, to commemorate their first 25 years as a Fairfax company.

"In commissioning this book, our goal was to celebrate the people and key events that have guided us to this special anniversary. While it is not intended to encompass every step of our journey, it does highlight many crucial moments during the past quarter century that have been important to our development and success.

"What has made our journey so rewarding? The answer is inside these pages, where many of our employees have expressed their thoughts and feelings about who we are as a company and what it's like to work at Odyssey in just six simple words. This six-word story challenge was posed in January 2020, and the response was overwhelming. I truly hope you enjoy reading them.

Brian Young – President and CEO Odyssey Group

Link to PDF copy of the book: https://odysseygroup.com/book/

Excess & Specialty - US Top 25 – 2022 & 2021

April 24, 2022

Fairfax has grown their excess and surplus lines insurance in the US by about 80% over the past 2 years. They were the 4th largest player in 2022, up from 7th in 2020.

What is excess and surplus lines insurance (E&S)?

Progressive explains it well on their web site:

> Excess and surplus lines (E&S) insurance is a market that protects high-risk businesses that standard insurers won't cover. This market is also known as surplus lines or non-admitted insurance.
>
> Companies with unusual or elevated risks often need E&S insurance because the admitted market considers them too risky to cover. These businesses could get a policy through a qualified E&S carrier.
>
> https://www.progressivecommercial.com/business-insurance/excess-and-surplus-insurance/

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Excess & Specialty - US Top 25 – 2022

Top US excess and surplus carriers see premiums surge, market share slip in 2022

"Fairfax Financial was the lone company among the top 10 that picked up market share in 2022, rising to 5.0% from 4.8%. The company also experienced a 26.6% surge in premiums."

Source S&P Global: https://www.spglobal.com/marketintelligence/en/news-insights/latest-news-headlines/top-us-excess-and-surplus-carriers-see-premiums-surge-market-share-slip-in-2022-75096783

Market share of leading US excess and surplus insurers in 2022

Rank			Market share (%)		Change	E&S DPW ($M)		Change
2022	2021	Insurer	2022	2021	(bps)	2022	2021	(%)
1	1	Berkshire Hathaway Inc.	9.2	9.4	-19	6,921.8	5,885.5	17.6
2	2	AIG	6.0	6.6	-63	4,536.6	4,177.5	8.6
3	3	Markel	5.1	5.6	-53	3,835.5	3,529.8	8.7
4	4	Fairfax Financial	5.0	4.8	24	3,781.0	2,995.9	26.2
5	5	W. R. Berkley Corp.	4.3	4.5	-21	3,251.5	2,841.8	14.4
6	7	Chubb	3.7	3.9	-20	2,778.1	2,439.7	13.9
7	6	Nationwide	3.7	4.1	-43	2,778.0	2,587.6	7.4
8	8	Liberty Mutual	3.0	3.5	-54	2,237.2	2,203.7	1.5
9	9	AXA SA	2.7	3.0	-33	2,024.2	1,895.7	6.8
10	10	Sompo	2.4	2.6	-16	1,821.5	1,616.7	12.7
11	11	STARR Cos.	2.4	2.3	12	1,819.5	1,438.6	26.5
12	14	AXIS	2.1	2.0	11	1,577.1	1,242.9	26.9
13	12	Tokio Marine	2.0	2.3	-28	1,498.5	1,426.1	5.1
14	20	Arch Capital	1.8	1.6	24	1,354.4	976.3	38.7
15	15	Zurich	1.8	1.9	-12	1,342.3	1,194.1	12.4
16	18	CNA	1.7	1.6	2	1,248.8	1,027.4	21.5
17	22	Munich Re	1.6	1.5	19	1,236.7	912.6	35.5
18	13	QBE	1.6	2.0	-42	1,227.7	1,284.5	-4.4
19	27	Trisura Group Ltd.	1.6	1.2	37	1,179.0	751.3	56.9
20	16	Everest Re	1.6	1.7	-13	1,175.0	1,063.2	10.5
21	19	Great American Insurance	1.5	1.6	-13	1,112.9	1,010.3	10.2
22	26	Kinsale Insurance Co.	1.5	1.2	24	1,101.6	764.0	44.2
23	21	The Hartford	1.4	1.5	-13	1,039.2	947.1	9.7
24	24	James River Group Holdings Ltd.	1.3	1.4	-10	982.7	884.4	11.1
25	23	Travelers	1.3	1.4	-16	968.6	906.0	6.9
		P&C industry	**100.00**	**100.00**		**75,513.1**	**62,900.8**	**20.1**

Data compiled April 13, 2023.
E&S = excess and surplus; DPW = direct premiums written.
Entities are deemed excess and surplus writers if they have active statuses of not licensed, eligible surplus lines or domestic surplus lines within Schedule T - Exhibit of Premiums Written
Data sourced from the State Pages or the Exhibit of Premiums and Losses within the annual property and casualty statutory statements filed with the NAIC. US filers only. Includes all 50 states and Washington, DC, but excludes US territories.
Insurer reflects consolidation of data from filers within SNL-defined corporate structures and unaffiliated companies.
Industry data excludes E&S premiums written through Lloyd's of London.
Source: S&P Global Market Intelligence.

Excess & Specialty - US Top 25 – 2021

Most top E&S insurers see market shares decline in 2021; premiums rise YOY

"Fairfax Financial Holdings Limited, the fourth-largest insurer in the rankings, was the only company among top 10 players to log a year-over-year increase in market share. The insurer's share of the E&S market rose to 4.77% from 4.50%. Fairfax Financial jumped two spots in the rankings, thanks to a 40% increase in premiums to $3.0 billion from $2.14 billion a year ago."

Source S&P Global: https://www.spglobal.com/marketintelligence/en/news-insights/latest-news-headlines/most-top-e-s-insurers-see-market-shares-decline-in-2021-premiums-rise-yoy-70287307

Market shares of leading US excess and surplus insurers in 2021

Rank			Market share (%)		Change	E&S DPW ($M)		Change
2021	2020	Insurer	2021	2020	(bps)	2021	2020	(%)
1	1	Berkshire Hathaway Inc.	6.72	7.49	-76	4,226.8	3,560.6	18.71
2	2	AIG	6.65	7.46	-82	4,177.5	3,549.4	17.69
3	3	Markel	5.61	5.87	-25	3,529.8	2,789.9	26.52
4	6	Fairfax Financial	4.77	4.50	27	2,995.9	2,140.4	39.97
5	4	W. R. Berkley Corp.	4.52	4.75	-23	2,841.8	2,260.6	25.71
6	5	Nationwide	4.12	4.67	-56	2,587.6	2,222.4	16.43
7	7	Chubb	3.88	4.07	-19	2,439.7	1,935.7	26.03
8	8	Liberty Mutual	3.51	3.59	-8	2,203.7	1,705.9	29.18
9	9	AXA SA	3.02	3.50	-48	1,895.7	1,663.1	13.99
10	10	Alleghany	2.64	2.70	-6	1,658.7	1,283.0	29.29
11	11	Sompo	2.57	2.49	8	1,616.7	1,186.3	36.29
12	13	STARR Cos.	2.29	2.27	2	1,438.6	1,081.0	33.08
13	16	Tokio Marine	2.27	1.97	30	1,426.1	937.8	52.07
14	15	QBE	2.04	2.02	3	1,284.5	959.5	33.87
15	17	AXIS	1.98	1.96	2	1,242.9	930.6	33.56
16	12	Zurich	1.90	2.35	-45	1,194.1	1,115.3	7.06
17	23	Everest Re	1.69	1.50	19	1,063.2	711.9	49.35
18	14	Argo	1.69	2.14	-45	1,062.0	1,015.5	4.58
19	21	CNA	1.63	1.54	9	1,027.4	734.5	39.87
20	18	Great American Insurance	1.61	1.64	-3	1,010.3	778.7	29.74
21	24	Arch Capital	1.55	1.47	8	976.3	698.5	39.76
22	19	The Hartford	1.51	1.58	-7	947.1	752.2	25.92
23	29	Munich Re	1.45	1.08	37	912.6	512.2	78.16
24	25	Travelers	1.44	1.43	1	906.0	682.5	32.75
25	20	James River Group Holdings Ltd.	1.41	1.55	-14	884.4	737.0	20.00
		P&C Industry	**100.00**	**100.00**		**62,866.1**	**47,561.7**	**32.18**

Data compiled May 5, 2022.
E&S = excess and surplus; DPW = direct premiums written
Entities are deemed excess and surplus writers if it has an active status of not licensed, eligible surplus lines or domestic surplus lines within Schedule T - Exhibit of Premiums Written.
Data sourced from the State Pages or the Exhibit of Premiums and Losses within the annual property and casualty statutory statements filed with the NAIC. U.S. filers only. Includes all 50 states and D.C., but excludes U.S. territories.
Insurer reflects consolidation of data from filers within SNL-defined corporate structures and unaffiliated companies.
Industry data excludes E&S premiums written through Lloyd's of London.
Source: S&P Global Market Intelligence

Chapter 7: Investments – Fixed Income

Fairfax has three economic engines that drive its earnings:

- Insurance
- Investments – fixed income
- Investments – equities/derivatives

In this chapter we are going to focus on the fixed income portfolio.

An Introduction to the Fixed Income Portfolio of Fairfax

November 25, 2023

The team: how does Fairfax manage fixed income?

All investments at Fairfax are managed through Hamblin Watsa.

> "Hamblin Watsa Investment Counsel, a wholly-owned subsidiary of Fairfax Financial Holdings Limited, provides global investment management services solely to the insurance and reinsurance subsidiaries of Fairfax." *Hamblin Watsa website*

Within Hamblin Watsa, the team that manages the fixed income portfolio is led by Brian Bradstreet. Brian has been with Fairfax for 36 years - from the very beginning.

<u>Is the team any good?</u>

Under Brian's leadership, the fixed income team at Fairfax has done an exceptional job over the decades of managing Fairfax's fixed income portfolio. They have a very good long term track record. I think we can say the fixed income team is a competitive advantage for Fairfax compared to peers. This is important because fixed income is by far the largest piece of Fairfax's total investment portfolio.

(As an aside, it was Brian Bradstreet who brought the CDS opportunity to Fairfax's attention just as the housing bubble got going in the US (2003?). By 2009, that investment had made Fairfax $2 billion in profit. Not too shabby.)

<u>How big is Fairfax's fixed income portfolio?</u>

Fairfax has an investment portfolio of about $57.5 billion. Of this total, about $16.5 billion or 29%, is invested in equities. The vast majority, about $41 billion or 71%, is invested in fixed income securities.

Fairfax Investment Portfolio		
September 30, 2023	**$bn**	**Split**
Fixed Income	$41.0	71%
Equities / Derivatives	$16.5	29%
Total Investments	**$57.5**	

When investors talk about Fairfax and investments, they usually focus exclusively on the equity holdings. The fixed income part of Fairfax is rarely discussed - even though it is the much larger part of the total investment portfolio.

Well, this is changing. Why? Follow the money…

Has the fixed income portfolio been growing in size?

The fixed income portfolio at Fairfax has increased from $20.3 billion at Dec 31, 2016 to an estimated $42 billion at Dec 31, 2023. The increase is $21.7 billion, or 107%. The CAGR from 2016 to estimated 2023 is 11%. With the expected closing of the GIG acquisition in Q4 and the continuation of the hard market we should see similar growth in 2024.

Fairfax: Fixed Income	
Nov 14, 2023	
	$bn
2016	$20.3
2017	$28.0
2018	$26.7
2019	$26.4
2020	$29.8
2021	$36.8
2022	$38.9
2023E	$42.0
2024E	$47.0

How much does Fairfax earn on its fixed income portfolio?

The returns that Fairfax earns in its fixed income portfolio come primarily in two ways:

- Interest income
- Investment gains (losses) - realized and unrealized

Fairfax actively manages its fixed income portfolio and has generated meaningful realized investment gains over time. However, to keep our analysis simple (and this post to a reasonable length), we are going to focus here on the largest bucket, interest income.

The historical returns for interest income

Interest income averaged $647 million per year from 2016-2021. From this average, it increased to an estimated $1.8 billion in 2023 or +182%. It is forecasted to increase further in 2024 to about $2.1 billion (my latest estimate).

The average yield on the fixed income portfolio from 2016-2021 at Fairfax was about 2.4%. The yield has almost doubled to an estimated 4.3% in 2023 and 4.6% in 2024.

Fairfax: Fixed Income				
Nov 14, 2023		Interest Income		
	$bn	$mn	/ Share	Yield
2016	$20.3	$514	$22	2.5%
2017	$28.0	$515	$19	1.8%
2018	$26.7	$744	$27	2.8%
2019	$26.4	$826	$31	3.1%
2020	$29.8	$717	$27	2.4%
2021	$36.8	$568	$24	1.5%
2022	$38.9	$874	$37	2.2%
2023E	$42.0	$1,826	$80	4.3%
2024E	$47.0	$2,140	$96	4.6%
Interest Inc - 2016-2021 avg $647mn/yr or 2.4%				

Summary

Fixed income investments are managed by a very capable team at Fairfax, lead by Brian Bradstreet. The fixed income portfolio has more than doubled in size from 2016 to 2023. At the same time the yield Fairfax is earning on its fixed income portfolio has almost doubled (from the average from 2016-2021). As a result of these two doubles (size and rate of return), interest income has spiked higher to about $2 billion per year (the current run rate).

Interest income is now the largest income stream at Fairfax. This is important because this source of income is considered to be very high quality by investors and analysts. It is considered to be high quality because it is relatively predicable and durable.

What happened to spike interest income so much? In short, over the past 2 years the fixed income team at Fairfax delivered a clinic in value investing and active management. But before we explore this further, let's first cover off some bond basics.

Fixed Income - Some Basics

November 25, 2023

Fixed income investing is very different from equity investing. Let's spend a few minutes and review a few things that are relevant to our analysis.

The greatest bull market in history.

From 1981-2020, bonds experienced the greatest bull market in history. It began in September 1981, when the interest rate on the 10-year US treasury peaked at around 16%. It ended 40 years later, in June 2020, when the interest rate on the 10-year US treasury bottomed at 0.65%. Ever falling interest rates was an incredible 40-year tailwind for fixed income investors (actually, all investors - equity, real estate etc).

The bull market lasted so long some of the risks of owning bonds, like interest rate risk, receded into the shadows…. largely forgotten by fixed income investors.

But everything changed in early 2022. The scourge of double digit inflation escaped from its cage and was wreaking havoc on the global economy. The Federal reserve and other central banks began a historic tightening cycle and, in the process, unleashed hell on bond markets.

The greatest bond bear market in history

From 2021-2023, bonds experienced the greatest bear market in their history. The interest rate on the 10-year US treasury - that had bottomed at 0.65% in 2020 - hit a 15 year high of 4.98% in October 2023. The relentless move higher in interest rates over the past 2 years has caused the value of fixed income portfolios to crater.

Where are the losses hiding? The massive losses are sitting on the balance sheets of central banks, pension funds and financial institutions all over the world. And yes, P/C insurance companies.

The Worst Bond Bear Market in History
October 13, 2023 by Ben Carlson

- https://awealthofcommonsense.com/2023/10/the-worst-bond-bear-market-in-history/

"One of the strange parts about living through the worst bond bear market in history is there doesn't seem to be a sense of panic. If the stock market was down 50% you better believe investors would be losing their minds. Yes, some people are concerned about higher interest rates but it feels pretty orderly all things considered.

"So why aren't people freaking out about bond losses more?

"It could be there are more institutional investors in long bonds than individuals. There are lots of pension funds and insurance companies that own these bonds.

"It's going to take a very long time for investors to get made whole but you can hold these bonds to maturity to get paid back at par."

Active management matters again

As the bear market in bonds clawed its way through fixed income portfolios, a few P/C insurance companies were much better prepared than others. To understand who the relative winners and losers were/are it is helpful to first review the risks of investing in bonds.

A review of some of the risks of investing in bonds

- Interest rate risk - rising interest rates cause bond prices to fall. Duration matters a lot with this risk. Spiking interest rates impact long duration bond portfolios much more than short duration portfolios.
- Credit risk - the risk the issuer may default on one or more payments. Market dislocations / recessions matter a lot with this risk - events that cause credit spreads to blow out. Commercial real estate (in particular office) has taken a beating over the past year.
- Inflation risk (purchasing power risk) - the risk that inflation is higher than the total return received on the bond. Unexpected inflation is what matters with this risk. Especially if the inflation is high and persists for years.
- Reinvestment risk - the risk that at maturity, the proceeds will be reinvested at a lower rate than the bond was earning previously.

What does all this mean for P/C insurers?

November 25, 2023

To state the obvious, how fixed income portfolios were structured in 2020 / 2021 - when interest rates bottomed - has determined how the bear market in bonds has impacted individual P/C insurers. The two key metrics were:

- duration
- credit quality

So far, the clear winners have been the P/C insurers that had fixed income portfolios in 2021/2022 that were low duration. (If we get an economic slowdown / recession then credit quality will likely also become an important factor.)

Interest rate risk

> "Only when the tide goes out do you discover who's been swimming naked." Warren Buffett

Most P/C insurers match the duration of their insurance liabilities with the duration of their fixed income portfolio. So, in 2020/2021, many P/C insurers had an average duration in their fixed income portfolios of about 4 to 4.5 years.

As a result of spiking interest rates in 2022, most P/C insurers saw the value of their fixed income portfolio plummet. This in turn caused book value to crater. This happened despite earning a strong underwriting profit in 2022.

P/C Insurance - Change in Book value Per Share				
			YOY Change	
December 31	**2022**	**2021**	**$**	**%**
Fairfax	$657.68	$630.60	$27.08	4%
WR Berkley	$25.52	$25.09	$0.43	2%
Intact Fin (C$)	$80.33	$82.34	-$2.01	-2%
Berkshire B	$214.80	$226.22	-$11.42	-5%
Markel	$929.27	$1,036.20	-$106.93	-10%
Chubb	$121.90	$139.99	-$18.09	-13%
AIG	$53.83	$79.97	-$26.14	-33%

Let's look at one P/C insurer to better understand what happened

Chubb is viewed by many investors/analysts as being one of the better run P/C insurers. At the end of 2020, Chubb's fixed income portfolio of $107.6 billion was sitting on an unrealized gain of $6.5 billion. Interest rates started to rise in 2021 and at year-end the fixed income portfolio was sitting on a smaller gain of $3.2 billion. In 2022, interest rates spiked higher. At the end of 2022, Chubb was suddenly sitting on a loss of $8.4 billion. Holy shit batman! The two year change in the fair value of

Chubb's fixed income portfolio was a staggering swing in value of $14.9 billion (from a gain of $6.5 to a loss of $8.4 billion). As a result, despite earning a strong underwriting profit, book value at Chubb got crushed in 2022.

To put this in context, from 2020 to 2022, Chubb earned an average of $3.5 billion per year in interest income from its fixed income portfolio. So, a $14.9 billion swing in value over 2 years is a big deal.

Chubb: Fixed income portfolio	Fair Value $bn	Cost $bn	(Losses) Gains $bn
2020YE	$107.6	$101.1	$6.5
2021YE	$106.9	$103.7	$3.2
2022YE	$98.6	$107.0	-$8.4

How did Fairfax manage to increase book value in 2022?

In terms of book value growth in 2022, Fairfax was a clear outlier. Why? In late 2021 Fairfax reduced the average duration of their fixed income portfolio to 1.2 years (more on this in a future post). As a result, it was not impacted by spiking interest rates nearly as much as other P/C insurers.

Did any other P/C insurers have extremely low duration?

Yes. Berkshire Hathaway had very low average duration (my guess is their loss in book value in 2022 was due in part to mark-to-market losses on their equity portfolio). WR Berkley also deserves a shout-out as their average duration at December 31, 2021, was 2.4 years, which was much lower than the average. As a result, in addition to Fairfax, WR Berkley was one of the few P/C insurers who were able to deliver an increase in book value in 2022.

How should we think about these losses?

Yes, big unrealized losses sound scary. Is this a solvency problem for P/C insurance companies? No, probably not. P/C insurers have said they will simply hold the bonds until they mature. Unless there is an unexpected liquidity need (perhaps like a 1-in-100 year catastrophe) it is unlikely we are going to see forced sales. So, if the losses will not be realized are they really a problem?

Given the sizeable impact to book value there may be regulatory implications - insurance regulators and credit rating agencies are likely paying close attention.

Perhaps the more important question is how long are some P/C insurers going to have to sit on those ~~shit~~ low yielding bonds they are holding? The key is duration. P/C insurers with fixed income portfolios with an average duration of 4 or 5 years are likely going to need another couple of years to get the low yielding bonds off their books. Low yielding bonds - means low interest income - means lower earnings.

P/C insurers with a low duration portfolio have a big earnings advantage for the next couple of years over P/C insurers with longer duration fixed income portfolios. We will discuss this more below.

Inflation risk

Expected inflation is generally not a problem. Unexpected inflation, if it is high and persistent, can be a big problem for P/C insurance companies. And guess what we have had for the past 2 years? Unexpected high (double digit) inflation.

Why is unexpected inflation an issue? Because most P/C insurance companies are sitting on tens of billions in insurance liabilities.

P/C insurers get paid a fixed amount up front when they write an insurance policy. When they price the policy, they have to guess at its cost. After doing all this, they hope to make a profit.

Unexpected inflation is a big problem for P/C insurers. It means costs are likely going up more than expected. This is especially problematic for long tail lines of business. Because those higher than expected losses keep happening for years into the future.

And if you also have a long duration fixed income portfolio - and, at the same time, you are stuck with ~~shit~~ low yielding bonds - well, your problems are even worse.

High unexpected inflation and a long duration / low yield fixed income portfolio is not a good combination for the profitability of a P/C insurer - it has the potential to squeeze earnings for years.

Perhaps this partly explains why the hard market that started in late 2019 kept going strong in 2023 and looks set to continue strong into 2024 - despite repeated predictions of its imminent demise.

Reinvestment opportunity (not risk)

The increase in interest rates the past 18 months has been historic in amount and speed. P/C insurers are seeing interest rates today - across the curve - at 15 year highs.

US Treasury Rates						
2021	**1 Month**	**1 Year**	**2 Year**	**3 Year**	**5 Year**	**10 Year**
31-Dec	0.06%	0.39%	0.73%	0.97%	1.26%	1.52%
2022	**1 Month**	**1 Year**	**2 Year**	**3 Year**	**5 Year**	**10 Year**
31-Mar	0.17%	1.63%	2.28%	2.45%	2.42%	2.32%
30-Jun	1.28%	2.80%	2.92%	2.99%	3.01%	2.98%
30-Sep	2.79%	4.05%	4.22%	4.25%	4.06%	3.83%
31-Dec	4.12%	4.73%	4.41%	4.22%	3.99%	3.88%
2023	**1 Month**	**1 Year**	**2 Year**	**3 Year**	**5 Year**	**10 Year**
31-Mar	4.74%	4.64%	4.06%	3.81%	3.60%	3.48%
30-Jun	5.24%	5.40%	4.87%	4.49%	4.13%	3.81%
30-Sep	5.55%	5.46%	5.03%	4.80%	4.60%	4.59%
18-Oct	5.58%	5.44%	5.19%	5.01%	4.95%	4.98%
21-Nov	5.52%	5.24%	4.86%	4.60%	4.41%	4.41%

P/C insurers with shorter duration fixed income portfolios have been able to capture the spike higher in interest rates much more quickly than P/C insurers with longer duration portfolios. We can see this by looking at the trend in interest income for the last 2 years.

Fairfax is estimated to see interest income increase 133% in 2023 and 222% over the past 2 years. Chubb, on the other hand, is estimated to see interest income increase 33% in 2023 and 47% over the past two years.

The speed of the earn-through for Fairfax is more than 4 x that of Chubb.

Earn-through in Interest Income	Fairfax			Chubb		
	$mn	**Change**	**2 Year Change**	**$mn**	**Change**	**2 Year Change**
2020YE	$717			$3,388		
2021YE	$568	-21%		$3,346	-1%	
2022YE	$784	38%		$3,717	11%	
E 2023YE	$1,827	133%	222%	$4,935	33%	47%
Fixed Income Portfolio						
Est 2023 YE	$42	bn		$107	bn	
Yield	4.4%			4.6%		

It is also interesting to note that the yield on both Fairfax's and Chubb's fixed income portfolio now looks remarkably similar. What is very different, however, is what they hold in their respective fixed income portfolios.

Credit Risk

The one risk I have not discussed is credit risk - the risk the issuer may default on one or more payments. Fairfax's fixed income portfolio is stuffed mostly with government bonds. High quality. Chubb? Very different.

The yield on Fairfax's and Chubb's fixed income portfolio might be similar. However, the credit risk (made up of the holdings in each of the two portfolios) looks very different to me. Which portfolio is riskier? Which portfolio should perform better it we see an economic slowdown? This post is long enough already… I'll let you answer those two questions on your own.

Conclusion

The historic bear market in bonds has crushed the value of fixed income portfolios of many P/C insurance companies - in turn this has cratered book value. But a few odd ducks were prepared - Fairfax, Berkshire Hathaway and WR Berkely. On a relative basis, over the past 24 months, P/C insurers with low duration fixed income portfolios have been the clear winners over P/C insurers with long duration fixed income portfolios. Fairfax was exceptionally well prepared.

Short duration portfolios protected book value. And the earn-through from higher interest rates (in the form of spiking interest income) has been much quicker - which is boosting profitability - compared to long duration peers.

Having a short duration portfolio has also provided valuable optionality - it allows P/C insurance companies to be opportunistic should we see any dislocations in financial markets (like April of 2023, and the crisis that hit regional banks in the US).

In my next post (coming next week), I will take a closer look at what the team at Fairfax has done with their fixed income portfolio over the past 2 years. What can we learn about Fairfax and their fixed income team? Does value investing also apply to bonds? Does active management matter?

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Background Information:

How P/C insurance companies account for their bond holdings is important for investors to understand.

Most bonds at most P/C insurance companies are held in the 'available-for-sale' bucket. This means that unrealized losses do not show up in earnings (or ROE calculations). However, these unrealized losses are real – instead, they show up in 'other comprehensive income' and book value.

How an Available-for-Sale Security Works

https://www.investopedia.com/terms/a/available-for-sale-security.asp#:~:text=Available%2Dfor%2Dsale%20(AFS,a%20ready%20market%20price%20available.

"Available-for-sale (AFS) is an accounting term used to describe and classify financial assets. It is a debt or equity security not classified as a held-for-trading or held-to-maturity security—the two other kinds of financial assets. AFS securities are nonstrategic and can usually have a ready market price available.

"The gains and losses derived from an AFS security are not reflected in net income (unlike those from trading investments) but show up in the other comprehensive income (OCI) classification until they are sold. Net income is reported on the income statement. Therefore, unrealized gains and losses on AFS securities are not reflected on the income statement.

"Net income is accumulated over multiple accounting periods into retained earnings on the balance sheet. In contrast, OCI, which includes unrealized gains and losses from AFS securities, is rolled into "accumulated other comprehensive income" on the balance sheet at the end of the accounting period. Accumulated other comprehensive income is reported just below retained earnings in the equitysection of the balance sheet."

The Genius of the Fixed Income Team at Fairfax

November 29, 2023

We are learning in real time the genius of the fixed income team at Fairfax. Genius is a big word, but I think it applies in this case. The team at Fairfax has been putting on a clinic for the past 3 years - demonstrating the significant value that active management can add to a fixed income portfolio.

We are going to look at what Fairfax has done the past 3 years in three parts:

- Part 1: Late 2021 - Getting even more defensive
- Part 2: 2022 - Start extending duration
- Part 3: 2023 - Being opportunistic and going on the offensive

Part 1: Late 2021 - Getting even more defensive

November 29, 2023

<u>The big picture</u>

We are taught the way to get rich in investing is to buy low and sell high. But sometimes the opposite can also work: sell high and then buy low.

In 2020 and 2021, the 40-year historic bond bubble reached its blow-off-top. Bond yields reached all-time lows and conversely bond prices reached all-time highs. Mr. Market was feeling positively euphoric when it came to fixed income investments - especially those that were long dated. What was a value investor to do? Why sell your long dated bonds of course.

<u>Below are details of 3 moves Fairfax made in late 2021:</u>

1.) Significant sales of corporate bonds at very low yields, locking in large, realized gains:

> "During 2021, we sold $5.2 billion in corporate bonds, mainly acquired in March/April of 2020, at a yield of approximately 1%, for a gain of $253 million." *Fairfax 2021AR*

The question to ask here is who was on the other side of this trade? Who was buying corporate bonds at a 1% yield in late 2021?

2.) The duration of the portfolio was shortened, and the composition of portfolio was shifted to higher quality holdings, mostly treasuries:

> "At the end of 2021, our fixed income portfolio, inclusive of cash and short-term treasuries, which effectively comprised 72% of our investment portfolio, had a very short duration of approximately 1.2 years and an average rating of AA-." *Fairfax 2021AR*

Most P/C insurance companies match the duration of their insurance liabilities with the duration of their fixed income investments - which is around 4 years. So Fairfax going to an average duration of 1.2 years with its fixed income portfolio was a significant difference compared to peers. Fairfax's move to mostly government bonds was also significant and another big difference compared to peers.

3.) Part of the fixed income portfolio was hedged to protect against rising interest rates:

> "To economically hedge its exposure to interest rate risk (primarily exposure to certain long dated U.S. corporate bonds and U.S. state and municipal bonds held in its fixed income portfolio), the company held forward contracts to sell long dated U.S. treasury bonds with a notional amount at December 31, 2021 of $1,691.3 (December 31, 2020 – $330.8)." *Fairfax 2021AR*

Fairfax did not sell all of its long dated bonds. It hedged some of its remaining exposure to provide added protection.

Summary

In late 2021, near the peak of the bond bubble, Fairfax 'sold high' and went extremely short duration with their massive fixed income portfolio of $37 billion. This positioning protected the company from the interest rate risk. It also protected them from inflation risk. Fairfax also shifted the vast majority of its fixed income portfolio to high quality government bonds, which protected the company from credit risk. In summary, by late 2021, Fairfax's fixed income portfolio was very defensively positioned.

The team at Fairfax made these move just months before the Fed (and other global central banks) unleashed hell on fixed income markets. With hindsight, Fairfax's timing was close to perfect. (It should be noted that Fairfax had been cautious on fixed income - expressed as low duration - since late 2016.)

Does value investing also apply to fixed income?

What Fairfax did was a good example of value investing. Long duration bonds, with crazy low yields in 2020 and 2021, provided no margin of safety. Especially later in 2021 when it was clear that the economy was expanding and inflation was quickly becoming a big problem.

Passive management versus active management

Most P/C insurers have a policy of blindly matching the duration of their insurance liabilities with the duration of their fixed income portfolio. So. in 2020 and 2021, other P/C insurers were busy buying 3 and 4 year bonds at historically low yields - they were buying at nose-bleed bubble high prices. Matching duration was the religion of the day. Yield did not matter.

This had been a winning strategy in a zero interest rate world - where interest rates and bond yields only ever went down. The problem with this strategy is it completely ignored interest rate risk and inflation risk. When the greatest bear market in history came lumbering along it crushed the value of fixed income portfolios of most P/C insurers. This in turn crushed the book value of most P/C insurers. Not Fairfax.

But we are getting a little ahead of ourselves. Back to late 2021.

Fairfax ended 2021 with 77% of its fixed income portfolio in 'cash', 'cash equivalents' and 'bonds of 1 year or less'. This was $28.4 billion of its $37.0 billion fixed income portfolio. This was a 'high conviction' move for Fairfax. (The increase in the 'Due after 10 years' bucket was due to the consolidation of Eurolife.)

	Fairfax Financial	**2020**		**2021**	
	Fixed Income Maturity Profile	**Fair**	**Amortized**	**Fair**	**Amortized**
	Bonds	**Value**	**Cost**	**Value**	**Cost**
1.)	Due in 1 year or less	$4,935	$4,968	$5,947	$6,023
	Due after 1 year through 5 years	$10,097	$9,378	$6,950	$6,674
	Due after 1 year through 3 years				
	Due after 3 years through 5 years				
	Due after 5 years through 10 years	$719	$654	$531	$534
	Due after 10 years	$545	$419	$1,106	$990
		$16,295	**$15,420**	**$14,534**	**$14,221**
	Pre-tax effective interest rate	3.2%		2.7%	
2.)	Cash and cash equivalents	$5,167		$12,749	
3.)	Short term investments	$8,471		$9,733	
	Total Fixed Income	**$29,932**		**$37,016**	
	Total 1 year or less (1 + 2 + 3)	$18,572		$28,429	
	% of total	62%		77%	

Having a short duration portfolio at the end of 2021 had two key benefits:

- It protected the balance sheet from interest rate risk - a rapid increase in interest rates would cause the value of bonds to plummet. This would then cause book value to fall. Long duration bonds were especially vulnerable.
- It provided valuable optionality - this would allow Fairfax to quickly take advantage of rising interest rates and dislocations in credit markets.

Part 2: 2022 - Start extending duration

November 29, 2023

The big picture

The big economic news in 2022 was the spiking of inflation and the subsequent aggressive tightening by the Fed and global central banks. This in turn caused interest rates to spike, especially short term interest rates. The greatest bond bear market in history accelerated as the year progressed.

US Treasury Rates

2021	1 Month	1 Year	2 Year	3 Year	5 Year	10 Year
31-Dec	0.06%	0.39%	0.73%	0.97%	1.26%	1.52%
2022	**1 Month**	**1 Year**	**2 Year**	**3 Year**	**5 Year**	**10 Year**
31-Mar	0.17%	1.63%	2.28%	2.45%	2.42%	2.32%
30-Jun	1.28%	2.80%	2.92%	2.99%	3.01%	2.98%
30-Sep	2.79%	4.05%	4.22%	4.25%	4.06%	3.83%
31-Dec	4.12%	4.73%	4.41%	4.22%	3.99%	3.88%

Fairfax's fixed income portfolio had an average duration of 1.2 years at Dec 31, 2021. With such a low duration portfolio, as interest rates spiked higher Fairfax saw interest income quickly increase. Interest income bottomed out at $130 million in Q4, 2021. A year later, in Q4, 2022, interest income increased to $314 million, an increase of 141%. The earn-through from higher interest rates was happening very fast for Fairfax.

Fairfax: Interest Income by Quarter

	Q1 $mn	Q2 $mn	Q3 $mn	Q4 $mn	FY $mn
2021	$153	$148	$137	$130	**$568**
2022	$153	$176	$230	$314	**$874**
Change	$0	$28	$93	$184	**$305**
%	0%	19%	68%	141%	**54%**

What did Fairfax do in 2022?

In 2022, Fairfax started extending the average duration of their fixed income portfolio - from 1.2 years at the end of 2021, to 1.4 years at the end of Q1, to 1.6 years at the end of 2022. Bonds at the short end of the curve (1-year to 3-year) offered the highest yield and this is where Fairfax bought aggressively.

Fairfax ended 2022 with 47% of its fixed income portfolio in 'cash', 'cash equivalents' and 'bonds of 1 year or less'. This was down significantly from 77%, where it ended 2021.

	Fairfax Financial Fixed Income Maturity Profile Bonds	2021 Fair Value	2021 Amortized Cost	2022 Fair Value	2022 Amortized Cost
1.)	Due in 1 year or less	$5,947	$6,023	$8,193	$8,507
	Due after 1 year through 5 years	$6,950	$6,674		
	Due after 1 year through 3 years			$15,686	$16,078
	Due after 3 years through 5 years			$4,117	$4,206
	Due after 5 years through 10 years	$531	$534	$291	$319
	Due after 10 years	$1,106	$990	$715	$860
		$14,534	**$14,221**	**$29,001**	**$29,969**
	Pre-tax effective interest rate	2.7%		3.6%	
2.)	Cash and cash equivalents	$12,749		$6,756	
3.)	Short term investments	$9,733		$3,292	
	Total Fixed Income	**$37,016**		**$39,049**	
	Total 1 year or less (1 + 2 + 3)	$28,429		$18,240	
	% of total	77%		47%	

Part 3: 2023 - Being opportunistic and going on the offensive

December 5, 2023

The big picture in 2023

The big news in 2023 was that aggressive tightening by global central banks continued. This was unexpected. This in turn caused interest rates to spike even higher.

The unexpected and historically rapid increase in interest rates also started to cause some dislocations in financial markets. Silicon Valley Bank and Signature Bank both went under in April. This created opportunities in credit markets.

In October of 2023, we saw long bond yields spike to 15-year highs. This provided an opportunity for short duration fixed income portfolios to extend duration.

US Treasury Rates

2021	1 Month	1 Year	2 Year	3 Year	5 Year	10 Year	
31-Dec	0.06%	0.39%	0.73%	0.97%	1.26%	1.52%	
2022	**1 Month**	**1 Year**	**2 Year**	**3 Year**	**5 Year**	**10 Year**	
31-Mar	0.17%	1.63%	2.28%	2.45%	2.42%	2.32%	
30-Jun	1.28%	2.80%	2.92%	2.99%	3.01%	2.98%	
30-Sep	2.79%	4.05%	4.22%	4.25%	4.06%	3.83%	
31-Dec	4.12%	4.73%	4.41%	4.22%	3.99%	3.88%	
2023	**1 Month**	**1 Year**	**2 Year**	**3 Year**	**5 Year**	**10 Year**	
31-Mar	4.74%	4.64%	4.06%	3.81%	3.60%	3.48%	
30-Jun	5.24%	5.40%	4.87%	4.49%	4.13%	3.81%	
30-Sep	5.55%	5.46%	5.03%	4.80%	4.60%	4.59%	
18-Oct	5.58%	5.44%	5.19%	5.01%	4.95%	4.98%	peak?
05-Dec	5.54%	5.06%	4.57%	4.33%	4.14%	4.18%	

What did Fairfax do in 2023?

1.) Fairfax was very opportunistic with the dislocation that hit regional banks in the US in March/April.

In March of 2023, Silicon Valley Bank went bankrupt. This was the second largest bank failure in US history. There was a run on the bank (depositors wanted their money) and SVB did not have it - the money was locked up in low-yielding long-dated US treasuries. To meet customer withdrawal requests, SVB was forced to sell its long-dated treasury holdings - and it was forced to book billions in losses. This then resulted in more customer withdrawal requests. To stop the vicious feedback loop, SVB was forced to declare bankruptcy and regulators from the Fed stepped in and closed the bank. Signature Bank was also shut down at the same time by regulators. A full blown financial crisis had emerged with regional banks being at the epicentre.

The cat pounces

As we have discussed, having a very high quality, low average duration fixed income portfolio provides important optionality. Wonderful opportunities that come up unexpectedly can be seized.

Many regional banks were forced to strengthen their balance sheets. To raise liquidity, PacWest Bancorp sold $2.6 billion in real estate construction loans to Kennedy Wilson. They were sold at a $200 million discount. KW's parter on the deal was Fairfax.

> "During the first nine months of 2023 the company, in partnership with Kennedy Wilson, has completed net purchases of $2.0 billion of first mortgage loans acquired from Pacific Western Bank; the average annual return on the capital deployed with the loans is expected to exceed 10%."
> *Fairfax Q3 Interim Report*

Fairfax was able to invest $2 billion of its fixed income portfolio at an expected annual return of 10%, or $200 million. Outstanding.

This deal also highlights another strength of Fairfax: the many partnerships it has built out over the years with many different external capital allocators. This deal was only possible because of the close relationship that Fairfax has with Kennedy Wilson - cultivated over the past 13 years.

2.) In 2023, Fairfax continued to push out the average duration of its fixed income portfolio. They did this in two stages: first, in Q1 and again in October.

In Q1, 2023, the average duration of Fairfax's fixed income portfolio was pushed out from 1.6 years to 2.5 years. This was more than a double from what it was 15 short months previously, at Dec 31, 2021.

It is instructive to look at the significant change in Fairfax's fixed income holdings over the past two years. You can see the shift to longer duration holdings.

	Fairfax Financial	2021		2022		Sept 30, 2023		
	Fixed Income Maturity Profile	Fair	Amortized	Fair	Amortized	Fair	Amortized	
	Bonds	Value	Cost	Value	Cost	Value	Cost	
1.)	Due in 1 year or less	$5,947	$6,023	$8,193	$8,507	$9,330	$9,542	*
	Due after 1 year through 5 years	$6,950	$6,674					
	Due after 1 year through 3 years			$15,686	$16,078	$10,492	$10,618	
	Due after 3 years through 5 years			$4,117	$4,206	$11,290	$11,463	
	Due after 5 years through 10 years	$531	$534	$291	$319	$3,057	$3,092	
	Due after 10 years	$1,106	$990	$715	$860	$458	$535	
		$14,534	**$14,221**	**$29,001**	**$29,969**	**$34,627**	**$35,250**	
	Pre-tax effective interest rate	2.7%		3.6%				
2.)	Cash and cash equivalents	$12,749		$6,756		$4,874		
3.)	Short term investments	$9,733		$3,292		$1,858		
	Total Fixed Income	**$37,016**		**$39,049**		**$41,359**		
	Total 1 year or less (1 + 2 + 3)	$28,429		$18,240		$16,063		*
	% of total	77%		47%		39%		

(*) Incl. 1st mortgage loans at Sept 30, 2023 of $4.6bn (Dec 31, 2022 - $2.5bn) secured by real estate in the U.S., Eur and Can.

3.) In Sept/Oct 2023, bond yields unexpectedly spiked higher - but this time it was further out on the on the curve - 5-year, 10-year and 20-year bonds.

We just learned on the Q3, 2023 conference call that in October, Fairfax has extended the average duration of its fixed income portfolio from 2.5 years to 3.1 years.

> "Recently, in October, during the spike in treasury yields, we have extended our duration to 3.1 years with an average maturity of approximately 4 years, and yield of 4.9%."
> *Prem Watsa - Fairfax Q3, 2023 Conference Call*

We will have to wait until Q4 earnings are released to get more complete details of what bonds Fairfax has purchased. This is a significant development for Fairfax and its shareholders. Bond yields have moved much lower in November and early December – Fairfax may have picked the perfect time to meaningfully extend the average duration of their fixed income portfolio and lock in very high bond yields for years.

What does all this mean for interest income at Fairfax?

Interest income was a record of $874 million in 2022. In 2023 it is forecasted to total $1.8 billion, an increase of $950 million or 109%. The earn-through has been very fast for Fairfax - much quicker than most P/C insurers.

My guess is Fairfax is currently earning about $500 million per quarter in interest income. And with the extension of duration, Fairfax has locked much of this in for years. For perspective, Fairfax earned $568 million in interest income for the entire year in 2021.

Fairfax: Interest Income by Quarter

	Q1 $mn	Q2 $mn	Q3 $mn	Q4 $mn	FY $mn
2021	$153	$148	$137	$130	**$568**
2022	$153	$176	$230	$314	**$874**
2023E	$362	$443	$492	$530	**$1,827**
YOY	$209	$267	$262	$216	**$954**
Change	136%	151%	114%	69%	**109%**

What have we learned in this post?

Capital allocation is the most important responsibility of a management team. Fixed income is by far the largest part of Fairfax's investment portfolio.

Over the past 3 years, the fixed income team has superbly navigated Fairfax (and Fairfax shareholders) through the greatest fixed income bubble top and subsequent bear market in history. This is yet another example of the outstanding performance we have seen from the management team at Fairfax in recent years.

They sold high - locked in nice gains and, most importantly, they avoided billions in losses. They protected the balance sheet. And then they bought duration on the cheap. They have also been very opportunistic, taking advantage of the high volatility in fixed income markets. And they did all this with a $40 billion portfolio.

Importantly, the fixed income portfolio at Fairfax looks to be very well positioned today. Fairfax has significantly pushed the average duration out - the table is now set for Fairfax to earn in the range of $2 billion in interest income in each of the next 3 years. The portfolio is also very high quality - heavily weighted to government bonds. Fairfax now likely owns the best 'risk-adjusted return' fixed income portfolio in the P/C insurance industry - it is both high yield and very high quality. And Fairfax is well positioned to continue to exploit continued volatility in fixed income markets.

In short, the fixed income team at Fairfax has just delivered a master-class in value investing and the benefits of active management. I think it is safe to say their performance has been best-in-class among P/C insurance companies.

This is just another meaningful example of 'the story' for Fairfax continuing to get better.

Can we quantify the benefit to Fairfax and its shareholders?

November 29, 2023

The benefits have come in two ways. The first has been the significant losses that have been avoided - let's call that balance sheet protection. The second is the significant and rapid increase in interest income.

1.) Balance sheet protection

One way to quantify the value here is to look at book value per share and compare Fairfax to other P/C insurance companies. How did Fairfax do compared to peers? I did this in my previous post so let's try another approach here.

Over the past three years, as the bear market in bonds was raging, many P/C insurers saw the value of their fixed income portfolios decline by double digit amounts. As an example, from Dec 31 2020 to Sept 2023, Chubb has seen a swing of $16 billion in the value of its $105 billion fixed income portfolio (from an unrealized gain of $6.5 billion at Dec 31, 2020, to an unrealized loss of $9.5 billion at Sept 30, 2023). This is a 15.2% swing in value for the fixed income portfolio.

Chubb: Fixed income portfolio			
	Fair Value $bn	**Cost $bn**	**(Losses) Gains $bn**
2020YE	$107.6	$101.1	$6.5
2021YE	$106.9	$103.7	$3.2
2022YE	$98.6	$107.0	-$8.4
Sept 30 2023	$105.2	$114.7	-$9.5

What about Fairfax?

From Dec 31, 2020 to Sept 2023, Fairfax has seen a swing in value of $1.5 billion in the value of its $41 billion fixed income portfolio (from an unrealized gain of $900 million to an unrealized loss of $600 million). As we learned above, Fairfax was aggressive in selling corporate bonds in 2021 locking in a gain of $250 million. So, its swing in value can be reduced to $1.25 billion. This is a 3% swing in value.

Fairfax: Fixed income portfolio			
	Fair Value $bn	Cost $bn	(Losses) Gains $bn
2020YE	$29.9	$29.1	$0.9
2021YE	$37.0	$36.7	$0.3
2022YE	$39.1	$40.0	-$1.0
Sept 30 2023	$41.4	$42.0	-$0.6

What if Fairfax had experienced the same swing in value as Chubb = 15.2%

Chubb is a good comparable and likely similar to what has been experienced by many P/C insurers.

On a $35 billion portfolio, a 12% swing in value would have equated to $4.2 billion. (Let's be conservative and use a lower swing number than Chubb's 15.2%.)

Fairfax saw an actual swing in value of $1.25 billion so the difference is $3 billion, or about $93/share after tax and minority interests. To be even more conservative, cut this number by 33% and it is still a massive number of $2 billion before taxes and minority interests.

The bottom line is Fairfax's decision to go extremely low duration in 2021 has benefitted the company and its shareholders in a big way. It protected the company's balance sheet. I think this benefit can be conservatively measured to have been in the billions.

2.) What was the increase in interest income

Interest income at Fairfax averaged about $650 million per year from 2016 to 2021. Fairfax is on track to earn more than $1.8 billion in 2023 and more than $2 billion in 2024. This is an increase of $1.3 billion or 200% over the trend from 2016 to 2021.

What is a new annual income stream of $1.3 billion worth? This is $58/share (yes, it is pre-tax and before minority interests).

Fairfax: Fixed Income				
Nov 14, 2023		Interest Income		
	$bn	$mn	/ Share	Yield
2016	$20.3	$514	$22	2.5%
2017	$28.0	$515	$19	1.8%
2018	$26.7	$744	$27	2.8%
2019	$26.4	$826	$31	3.1%
2020	$29.8	$717	$27	2.4%
2021	$36.8	$568	$24	1.5%
2022	$38.9	$874	$37	2.2%
2023E	$42.0	$1,826	$80	4.3%
2024E	$47.0	$2,140	$96	4.6%
Interest Inc - 2016-2021 avg $647mn/yr or 2.4%				

Summary

The benefits to Fairfax (and Fairfax shareholders) of how the company has managed its fixed income portfolio over the past 3 years can be measured in the $billions. It is impossible to come up with a precise number. What we do know is the value creation has been significant.

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Narrative: My guess is most investment professionals have a strong opinion about Fairfax. Ask these same people to explain to you what Fairfax has done with their fixed income portfolio over the past 3 years and my guess is only 1 in 10 would be able to provide an accurate/satisfactory answer. That partly explains why narratives on a company can be completely wrong at times. Most investment professionals don't follow companies all that closely. Usually, they don't need to.

But the fundamentals matter. Eventually investors do figure it out. And the narrative slowly gets updated (and brought closer to reality). And the stock price as well.

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Family control: At the Fairfax AGM this year (April 2023), a bunch of Fairfax shareholders met at the Keg one night for dinner and Ben Watsa came by for a visit and to say a few words. He commented about the positioning of the fixed income portfolio in 2021 (very low duration) and suggested this might be a good example for Fairfax shareholders of the benefit of family control.

With family control, it is easier for Fairfax to accept quarterly volatility and instead run the business with a long term focus. (Please note, these are my words and not Ben's.)

What do Fairfax, Berkshire Hathaway, Markel and WR Berkley all have in common? They are all P/C insurers (float is a beautiful thing). They all have exceptional long term track records of compounding shareholder value. And they are all family controlled. The last point might be the most important.

Chapter 8: Investments – Real Estate

Fairfax has been increasing its exposure to real estate in recent years. This is primarily being done though their close partnership with Kennedy Wilson. Fairfax also picked up some real estate assets as part of the Toys "R" Us purchase in April of 2018 (Fairfax purchased the Canadian operations of Toys "R" Us out of bankruptcy and then sold the retail operation in Aug 2021 and kept the real estate assets). Recipe (84% owned by Fairfax) also has some real estate in its portfolio of assets that were acquired as part of the St-Hubert acquisition in March of 2016.

Fairfax also has exposure to real estate in Greece through its ownership of Grivalia Hospitality. Eurobank also has significant real estate holdings that were acquired when it merged with Grivalia Properties in 2019.

Kennedy Wilson (KW)

Update December 8, 2023

On December 6th Kennedy Wilson made two regulatory filings than involved Fairfax.

1.) Kennedy Wilson and Fairfax increased their commitment to the KW debt platform by $2 billion, from $8 billion to $10 billion.

"On December 6, 2023, Fairfax Financial Holdings Limited, a company organized under the laws of Canada ("Fairfax"), and a current partner of Kennedy-Wilson Holdings, Inc. (the "Company"), has increased its first mortgage commitment within the Company's debt investment platform by $2 billion to $10 billion (the "Commitment"), bringing total commitments under the Company's global debt platform with all investors to $11 billion. Pursuant to the terms of the Commitment, such funds will constitute non-discretionary capital, with each investment on the platform continuing to be subject to Fairfax's review and approval. The Company expects to continue to hold approximately 2.5% equity interest in future debt investments within the platform while earning customary fees in its role as asset manager. As of September 30, 2023, the Company held interests in 98 loans, located in the United States and the United Kingdom, with an unpaid principal balance ("UPB") of $4.7 billion of real estate debt (of which the Company's share was a UPB of $256 million). Under these loans, the Company and its partners have future funding commitments of $1.8 billion (of which the Company's share is $93 million)."

https://otp.investis.com/clients/us/kennedy_wilson1/SEC/sec-show.aspx?Type=html&FilingId=17105435&CIK=0001408100&Index=10000

2.) The two preferred stock / warrant agreements Fairfax recently signed with Kennedy Wilson in 2022 and 2023 were amended to allow Fairfax to own up to 27.5% of KW stock (up from 20%).

> "The amendment primarily provides for an increase to Fairfax's cap on purchases of any of the Company's common stock, or other equity-linked securities, from 20% of the Company's fully diluted common stock to an amount not to exceed (x) the beneficial ownership… of 27.5% of the total voting power of the Company's voting stock nor (y) 27.5% of the Company's fully diluted common stock. As a result of the amendments to the SPAs, Fairfax will be permitted to purchase additional shares of the Company's common stock in the open market. There can be no assurance that Fairfax will make any such purchases."
>
> https://otp.investis.com/clients/us/kennedy_wilson1/SEC/sec-show.aspx?Type=html&FilingId=17105470&CIK=0001408100&Index=10000

August 1, 2023

Kennedy Wilson is a misunderstood and underappreciated part of Fairfax's investment portfolio. Most investors look at Kennedy Wilson through the lens of an equity holding. Looking at the performance of KW's stock price the past 5 years… what a dog! Woof! KW shares were trading around $21.40 five years ago and today they closed at $16.44/share.

What a terrible investment by Fairfax. Right? Wrong.

Kennedy Wilson has been one of Fairfax's best investments. What is wrong with the analysis above? It completely misses the point of WHY Fairfax invested in KW in the first place (and remains invested) – it was/is to tap into Kennedy Wilson's extensive global real estate expertise.

First, let's do a quick review.

Fairfax began its relationship with Kennedy Wilson in 2010. A very successful real estate investment partnership has recently blossomed to now include a significant real estate debt platform. Over the past 3 years, Kennedy Wilson has become a much more important part of Fairfax's investment portfolio. The partnership now includes both equity and fixed income investments:

- 2010: $100 million direct investment in Kennedy Wilson stock
- 2010: Real estate investment partnerships
- 2020: Real estate debt platform
- 2022: $300 million debenture (4.75%)
  - 7-year warrants for 13 million common shares with strike price of $23.
- 2023: Purchase of $2.3 billion in real estate loans from PacWest.
- 2023: $200 million debenture (6%)
  - 7-year warrants for 12.3 million common shares with strike price of $16.21

How much does Fairfax currently earn annually from its different investments with KW?

My very rough estimate is around $481 million. Fairfax has about $5.7 billion invested with Kennedy Wilson so this represents about an 8.4% annual rate of return for Fairfax.

Of this total, about $429 million is interest and dividends. The PacWest loan transaction just closed so the incremental earnings from this investment will start to show in the interest and dividend income bucket starting in Q3.

Kennedy Wilson					
Estimate of the amount earned annually by Fairfax across all KW investments					
01-Aug-23					
		Amount	**Rate**	**Total $**	**Total $**
Real Estate Debt Platform		$2,400	7.9%	$189.6	$189.6
PacWest Loan Portfolio		$2,000	10%	$200.0	$200.0
Total Interest Earned					**$389.6**
			Dividend		**Annual**
		Shares	**$ / Share**	**Total $**	**Total $**
Dividend	Common Stock	13.3	$0.24	$3.2	$12.8
		amount	**rate**	**Total $**	
Debentures	2022	$300	4.75%	$14.3	$14.3
Debentures	2023	$200	6%	$12.0	$12.0
Total Dividend Earned					**$39.0**
		Shares	**Strike**	**KW stock**	
		Million	**Price**	**01-Aug-23**	**Total $**
Warrants	2022	13	$23.00	$16.44	$0.0
Warrants	2023	12.3	$16.21	$16.44	$2.8
Legacy Real Estate Investment Partnership - rough estimate					$50.0
Total Investment Gains - rough estimate					**$52.8**
Total - Interest and Dividends					**$428.6**
Grand Total - Estimated amount earned across all KW investments					**$481.4**

The expansion of the relationship with Kennedy Wilson provides another good example of how Fairfax, over the last 5 years, has been:

- Leveraging and expanding existing, successful, long-term partnerships.
- Methodically diversifying their investment portfolio - in this case into real estate.

The result is yet another new, growing, significant and steady stream of earnings for Fairfax.

What is the timeline of Fairfax's various investments in/with Kennedy Wilson?

Started in 2010

- Kennedy Wilson (KW) stock
    - Initial equity investment was US$100 million (9% of company).
    - Today position is worth $200 million (13.3 million shares x $14.98/share).
    - Current annual dividend of $0.96 = 6.4% yield = $12.8 million in dividend income per year.
    - Wade Burton is on the board (along with Stanley Zax, who sold Zenith to Fairfax in 2010).
- investment partnership:
    - Started with $278 million in 2010.
    - Prem's 2022 letter: "we have invested $1.2 billion alongside with them in real estate, have received cash proceeds of $1.1 billion and still have real estate worth about $570 million. Our average annual realized return on completed projects is approximately 22%."

Expanded in 2020

- Launched a real estate debt platform: to pursue first mortgage loans secured by high-quality real estate in the Western U.S., Ireland and the U.K.
    - 2020, initial amount of $2 billion.
    - 2022, increased to $5 billion
    - Prem's 2022 letter: "$2.4 billion invested through Kennedy Wilson in well-secured first mortgages, primarily on high quality residential apartment buildings, at a floating rate (currently 7.9%)" = $190 million in interest income.

Expanded further in 2022

- 2022: KW perpetual preferred equity investment = $300 million
    - Pays an annual dividend of 4.75% = $14.25 million.
    - Includes 7-Year warrants for 13 million shares at strike price of $23/share.

Expanded further in 2023

- PacWest debt purchase of $2.3 billion: KW is buying loans at a discount for $2.1 billion, of which Fairfax is buying $2 billion (95%). Fairfax is also assuming $1.7 billion in future funding obligations.
    - Average loan to value is 51%.
    - More than 70% of the loans relate to multifamily or student residences; the remainder are a mix of industrial, hotel and life sciences office property projects.
    - Fairfax expects the average annual return to exceed 10%.
    - Remaining term to maturity is 1.7 years, with some loans carrying extension rights (max 2 years).

- 2023: KW perpetual preferred equity investment = $200 million

    - Pays an annual dividend of 6% = $12 million.
    - Includes 7-Year warrants for 12.3 million shares at strike price of $16.21/share.

Ownership of stock:

- Kennedy Wilson has 139.4 million shares outstanding.
- Fairfax owns 13.3 million = 9.5%
- Fairfax also owns warrants:
    - 13 million at $23
    - 12.3 million at $16.21
- If Fairfax exercises all warrants it would own 38.6 million shares = 23.4% (of 164.7 total)

Fairfax is getting paid 4.75% and 6% while waiting for the warrants to get in the money (they have seven years).

What does Fairfax see in Kennedy Wilson?

Prem's comment from the 2022 press release from Kennedy Wilson announcing the PacWest transaction:

"We are pleased to make this new investment in Kennedy Wilson and to build on our outstanding partnership that dates back to 2010," said Prem Watsa, Chairman and CEO of Fairfax. "We believe in their global business model, the strength of their high-quality, income-generating assets, and their best-in-class management team." *Prem Watsa – 2022 Presse Release from Kennedy Wilson*

To learn more about Kennedy Wilson:

Company web site: https://ir.kennedywilson.com

Q4 2022 Investor Presentation: https://ir.kennedywilson.com/~/media/Files/K/Kennedy-Wilson-IR-V2/reports-and-presentations/presentations/q4-2022-investors-presentation.pdf

Interesting trivia point: Bill McMorrow (CEO and Chairman of KW) was the genesis behind Fairfax's investment in Bank of Ireland in 2011. Fairfax made around $1 billion from that one investment. Thank you, Bill! (see Prem's comments below from 2011AR)

Related Source Material

2020: Kennedy Wilson and Fairfax Launch New $2 Billion Real Estate Debt Platform

"Kennedy Wilson and Fairfax first invested together in 2010 when the two companies acquired $250 million of real estate assets, including real estate secured loans and real property. Over the past decade, the companies have partnered on $7 billion in aggregate acquisitions, including over $3 billion of real estate related debt investments. In addition, Fairfax currently has an equity ownership interest in Kennedy Wilson of approximately 9%."

https://ir.kennedywilson.com/news-events-and-presentations/press-releases/2020/05-14-2020-105955816

2022: KW Announces $300 Million Perpetual Preferred Equity Investment From Fairfax Financial

"Kennedy Wilson and Fairfax began their relationship in 2010 when Fairfax made a $100 million equity investment in Kennedy Wilson. Over the past decade, the companies have partnered on $8 billion in aggregate acquisitions, including approximately $5 billion of real estate related debt investments. Fairfax currently has an equity ownership interest in KW of approximately 9%."

https://ir.kennedywilson.com/news-events-and-presentations/press-releases/2022/02-23-2022-211613501

2023: Fairfax Financial Partners With Kennedy Wilson to Acquire Loan Portfolio From Pacific Western Bank, Makes Additional Equity Investment in Kennedy Wilson

https://www.fairfax.ca/press-releases/fairfax-financial-partners-with-kennedy-wilson-to-acquire-loan-portfolio-from-pacific-western-bank-makes-additional-equity-investment-in-kennedy-wilson-2023-06-05/

Kennedy Wilson's Press Release

"The acquisition of this Loan Portfolio from Pacific Western Bank highlights Kennedy Wilson's historic ability to find off-market transactions during periods of uncertainty, move with speed, and build on our successful track record of investing through all real estate cycles," said William McMorrow, Chairman and CEO at Kennedy Wilson. "The foundations of Kennedy Wilson are our deep relationships, our reputation as a great partner, and our strength in being nimble when opportunity arises; all of which came into play with this loan portfolio acquisition."

https://ir.kennedywilson.com/news-events-and-presentations/press-releases/2023/06-09-2023-110020523

Prem's comments about Kennedy Wilson from Fairfax's 2022AR.

"Since we met Bill McMorrow and Kennedy Wilson in 2010, we have invested $1.2 billion alongside with them in real estate, have received cash proceeds of $1.1 billion and still have real estate worth about $570 million. Our average annual realized return on completed projects is approximately 22%. We also own 10% of the company. More recently we have been investing with Kennedy Wilson in first mortgage loans secured by high quality real estate in the western United States, Ireland and the United Kingdom with a loan-to-value ratio of 60% on average. At the end of 2022, we had invested in $2.0 billion of mortgage loans in the U.S. at an average yield of 8.1% and an average maturity of 1.7 years, and in approximately $350 million of mortgage loans in the U.K. and Europe at an average yield of 6.0% and an average maturity of 2.5 years." *Prem Watsa – Fairfax 2022AR*

"The combination of interest and dividends and profit from associates accounted for a 3.7% return on our portfolio in 2022, the highest return in the last five years (average 2.5%). We expect to earn these returns in 2023 as well, partly because we have $2.4 billion invested through Kennedy Wilson in well-secured first mortgages, primarily on high quality residential apartment buildings, at a floating rate (currently 7.9%)." *Fairfax 2022AR*

Fairfax's comments about KWF LP partnerships from Fairfax's 2013AR.

"The KWF LPs are partnerships formed between the company and Kennedy-Wilson, Inc. and its affiliates to invest in U.S. and international real estate properties. The company participates as a limited partner in the KWF LPs, with limited partnership interests ranging from 50% to 90%. Kennedy-Wilson holds the remaining limited partnership interests in each of the KWF LPs and is also the General Partner. For the KWF LPs where the company may exercise veto rights over one or more key activities, those partnerships are considered joint ventures under IFRS 11. Where the company has no veto rights over key activities, the company is considered to have significant influence under IAS 28. The equity method of accounting is applied to all of the KWF LPs." *Fairfax 2013AR*

Prem's comments about Kennedy Wilson from Fairfax's 2011AR.

"I have attended the Berkshire Hathaway shareholders' meeting since there were only 200 shareholders in attendance about 30 years ago. I still find I learn something each year from Warren and Charlie. At the meeting in 2010, I met Bill McMorrow through Alan Parsow, who is a money manager based in Omaha and a great friend. Bill founded Kennedy Wilson, a real estate services and investment company, in 1988, and he now owns 26% of the company. As a result of this meeting, we invested $100 million in a Kennedy Wilson 6% preferred convertible at $12.41 per share, and later purchased $32.5 million of a 6.45% preferred convertible at $10.70 per share and 400,000 common shares at $10.70 per share. Fully diluted we own 18.5% of the company. In 2010 and 2011, we also invested $290 million in several real estate deals with Kennedy Wilson in California, Japan and the U.K. – deals at significant discounts to replacement cost and with excellent unlevered cash on cash returns, in which Kennedy Wilson is the managing partner and a minority investor. We are thrilled to be partners with Bill and his team, who always focus on the downside and have the expertise to manage these investments and finally harvest them. You never know what you will find at a Berkshire meeting!!"

"And there is more to the McMorrow story. While Bill was negotiating the purchase of some real estate loans from Bank of Ireland, he was really impressed with Ritchie Boucher, the Bank's CEO. Bill introduced Ritchie to us, and we too were very impressed. With the help of our friends at Canadian Western Bank, one of the best banks in Canada, we thoroughly reviewed the opportunity and then quickly formed an investment group with Wilbur Ross, Mark Denning from Capital Research and Will Danoff at Fidelity, which purchased $1.6 billion of Bank of Ireland shares on a rights issue (Fairfax's share was $387 million)." *Prem Watsa – Fairfax 2011AR*

Grivalia Hospitality

May 22, 2023: News Article on Grivalia Hospitality

Grivalia Hospitality: Greek Luxury Tourism, Glamping Projects Coming Soon

https://news.gtp.gr/2023/05/22/grivalia-hospitality-greek-luxury-tourism-glamping-projects-coming-soon/

August 2, 2023

In July of 2022 Fairfax invested $194.5 million to purchase 44.9% of Grivalia Hospitality. This purchase increased Fairfax's ownership from 33.5% to 78.4%. I believe Fairfax purchased this stake from Eurobank.

"On July 5, 2022 the company increased its interest in Grivalia Hospitality S.A. ("Grivalia Hospitality") to 78.4% from 33.5% by acquiring additional shares for cash consideration of $194.6 million (€190.0 million). The company will commence consolidating Grivalia Hospitality in the third quarter of 2022. Grivalia Hospitality acquires, develops and manages hospitality real estate in Greece, Cyprus and Panama." *Fairfax Q2-2022 Earnings Release*

On December 31, 2022, what was the value of Fairfax's position in Grivalia Hospitality?

- Carrying value = $411 million
- Market value = $409 million (represents Fairfax's recent transaction valuation)

Who is Grivalia Hospitality?

"Our goal is to generate superior risk-adjusted returns for our shareholders, through targeted investments in the high-end hospitality sector. Our investments integrate disciplined acquisition criteria, value-adding investment strategies, development capabilities and excellent relationships with high-end global brands." *Grivalia Hospitality web site*

Link to company web site: https://grivaliahospitality.com

The shareholders of Grivalia Hospitality are:
- Grivalia Management Company
- Eurobank
- Fairfax (78.4%)

Why did Fairfax make this investment?

It looks to me like this was a 'bet on the jockey,' George Chryssikos. George is an expert on Greek real estate, and he has made Fairfax a great deal of money over the past decade.

Prem's comments about Grivalia Hospitality from Fairfax's 2022AR.

"Recognizing the outstanding results achieved at Grivalia Hospitality by George Chryssikos, Vice Chair of Eurobank, in 2022 we increased our ownership to 78%. Grivalia Hospitality is a leading investor in Greece's booming ultra- luxury hotel space, with three operating assets and seven under development. You will remember that George ran Grivalia Properties, a public company of which we owned 51%. Eurobank and Grivalia Properties merged in 2019 when Eurobank needed capital. The gains from Grivalia Properties and the Eurobank shares we acquired on the merger have resulted in a total gain to Fairfax of approximately $1 billion. We gratefully add George's name to Richie Boucher's from the Bank of Ireland, who was our first billion dollar man."

Prem Watsa – Fairfax 2022AR

If this is a bet on the jockey, then who is George Chryssikos?

Below is George's bio from the Grivalia Hospitality web site:

George Chryssikos (Chairman & CEO

- George Chryssikos has founded Grivalia Hospitality platform in 2015 to deploy capital in the very attractive high-end hospitality sector in Greece and abroad. The company has already invested in seven hospitality assets with an estimated value of over €0.5 bn and it is managed by Grivalia Management Company.
- George Chryssikos founded Grivalia Management Company and has an active leading and managing role. At this moment Grivalia has € 3.1 bn of assets under management and continues capital deployment in the Greek real estate sector.
- George served as Chief Executive Officer, Executive BoD member and Chairman of the Investment Committee of Grivalia Properties REIC. Together with his team, George has completed real estate transactions of over €1.2 bn in commercial and leisure real estate.
- George is currently Vice Chairman, Non-Executive Director of the BoD of Eurobank Group. In the past George was Managing Director of Corporate Value Partners, CEO of DTZ in Greece, BoD advisor at Iaso Healthcare Group and Senior Associate in McKinsey & Co at the London Office specializing in private equity. He has also experience in the construction industry in Greece, having worked as Project manager for more than 2 years in a specialized construction company.
- George holds an MBA in Corporate Finance & Strategy from Columbia Business School (NY), an MSc in Engineering & Construction Management from UC Berkeley (CA) and a MEng in Civil Engineering from National Technical University of Athens. In his younger age, George was a National Champion in sailing and member of the Greek National Sailing Team for many years.

Grivalia Properties – A look into the past

To understand Grivalia Hospitality is it good to go back in time and start with Grivalia Properties.

For a historical look at Fairfax's investment in Grivalia Properties go to 'Chapter 12: Geographies' and read the two posts on Greece.

The presentation below by George Chryssikos is a good review of Grivalia Properties.

Greek Centre for Value Investing Conference – October 24, 2022

Topic: 'The Grivalia Story'

- Presenter: George Chryssikos, Vice Chairman, Eurobank Group
- View PowerPoint Presentation
- View YouTube Presentation (sorry, sound quality is terrible but if you hang in there you can learn a great deal about how George's mind works – the guy is wicked smart)

Some takeaways:

1.) On page 8 of the presentation, it states Fairfax earned a return of 24% per year from 2011-2020 on its investment in Grivalia Properties. From its initial purchase to when Grivalia Properties merged with Eurobank. Pretty good.

2.) I wonder what else Fairfax owns that we know nothing about. Prior to the Q2-2022 release, I never knew they owned a large chunk of Grivalia Hospitality.

3.) With a total value of about $400 million, Grivalia Hospitality is now a top 10 equity investment for Fairfax.

4.) The investment of $195 million in Grivalia Hospitality is significant:

- Take advantage of weak Euro (to US$).
- Increase exposure to real estate - considered a good inflation hedge.
- Hospitality segment - high net worth individuals (trophy properties).
- Bet on Greece – continued economic expansion.

5.) The majority of Fairfax's spending on new investments the past two years has been going to increasing positions in businesses they already own a large stake in and therefore understand very well.

Chapter 9: Investments – Equities – General Posts

Change in value of Fairfax's equity portfolio in Q1 - 2024

March 31, 2024

Fairfax's equity portfolio (that I track) had a total value of about $19 billion at March 31, 2024. This is an increase of about $585 million (pre-tax) or 3.2, which is a solid start to 2024.

Fairfax: Equity Portfolio - Q4 Performance				
Split by Accounting Treatment	**Mar 31**	**Dec 31**		
A.) Mark to market	$ 9,089	$ 8,699	$ 390	4.5%
B.) Associates	$ 6,931	$ 6,812	$ 119	1.7%
C.) Consolidated	$ 2,949	$ 2,872	$ 76	2.7%
Total Equity Portfolio	**$18,968**	**$18,383**	**$ 585**	**3.2%**

I include the FFH-TRS position in the mark to market bucket and at its notional value.

My tracker portfolio is not an exact match to Fairfax's actual holdings. My summary has been updated to include information from Fairfax's 2023 annual report.

My tracker portfolio is useful only as a tool to understand the rough change in Fairfax's equity portfolio (and not the precise change).

Split of total holdings by accounting treatment

About 48% of Fairfax's equity holdings are mark to market - and will fluctuate each quarter with changes in equity markets. The other 52% are Associate and Consolidated holdings.

Over the past couple of years, the share of the mark to market portfolio has been shrinking. This means Fairfax's quarterly results will be less impacted by volatility in equity markets.

Fairfax: Equity Portfolio: Split by Accounting Treatment				
	March 31, 2023		**Own / control**	
A.) Mark to market	$ 9,089	48%	Own < 20%	
B.) Associates	$ 6,931	37%	Own 20 to 50%	Significant influence but not control
C.) Consolidated	$ 2,949	16%	Own > 50%	Control
Total Equity Portfolio	**$18,968**	**100%**		

Split of total gains by accounting treatment

- The total change is an increase of $585 million = $25.45/share
- The mark to market change is an increase of $390 million = $16.96/share. The change in this bucket of holdings will show up in 'net gains (losses) on investments' (along with changes in the value of the fixed income portfolio) when Fairfax reports results each quarter.

Fairfax: Performance of Equity Portfolio in Q1 - 2024		
	Dec 31 '23 to Mar 31 '24	
Split by Accounting Treatment	**Total US$**	**Per Share**
A.) Mark to market	$ 390	$16.96
B.) Associates	$ 119	$5.17
C.) Consolidated	$ 76	$3.32
Total Increase	**$ 585**	**$25.45**

What were the big movers in the equity portfolio Q1-YTD?

- The FFH-TRS is up $311 million. This position is now Fairfax's second largest holding.
- Eurobank is up $184 million and it is now Fairfax's largest equity holding at $2.4 billion.
- Micron Technology is up $127 million. It is now a top-10 holding at $461 million.
- Thomas Cook India is up $108 million. TCIC continues its strong performance.
- Commercial International Bank is down $118 million. Egypt devaluated its currency 40% on March 7. It is a well run bank. Country is an economic mess.

Fairfax: Big Movers in the Equity Portfolio Q1 - 2024		
Dec 31 '23 to Mar 31 '24	**Change**	**Accounting Treatment**
FFH Total Return Swap	$ 311	Mark to market
Eurobank	$ 184	Associates
Micron Technology	$ 127	Mark to market
Thomas Cook India	$ 108	Consolidated
Orla Mining	$ 88	Mark to market
Occidental Petroleum	$ 29	Mark to market
Commercial Intnl Bank (Egypt)	$ (118)	Mark to market
Stelco	$ (64)	Associates
Kennedy Wilson	$ (51)	Mark to market
Blackberry	$ (36)	Mark to market
Total Increase	**$ 585**	

Excess of fair value over carrying value (not captured in book value)

For Associate and Consolidated holdings, the excess of fair value to carrying value is about $1,206 million or $52/share (pre-tax). Book value at Fairfax is understated by about this amount.

- Associates: $722 million = $31/share
- Consolidated: $484 million = $21/share

Equity Tracker Spreadsheet explained:

We have separated holdings by accounting treatment: mark to market, associates – equity accounted, consolidated, other Holdings – total return swaps.

We come up with the value of each holding by multiplying the share price by the number of shares. Are holdings are tracked in US$, so non-US holdings have their values adjusted for currency.

This spreadsheet contains errors. It is updates as new and better information becomes available.

	Fairfax Financial - Summary of Equity Holdings (Page 1 of 2)									23.0	
				$ US Market Value					owned	Local Currency	
	A.) Equities - Mark to Market		own	Total	Total	Change		Carrying	shares	2023	
	Ticker	Stocks	%	31-Mar	31-Dec	(mill $)	%	Value	(million)	31-Mar	31-Dec
$US	OXY	Occidental Petroleum	1.0%	$ 357	$ 328	$ 29	9%		5.5	$ 64.99	$ 59.71
EUR	MYTIL.AT	Mytilineos	6.7%	$ 259	$ 272	$ (13)	-5%		6.7	€ 35.76	€ 36.70
$US	MU	Micron Tech	0.7%	$ 461	$ 334	$ 127	38%		3.912	$117.89	$ 85.34
EGP	EGS60121(	Com Int Bank - Egypt	7%	$ 362	$ 480	$ (118)	-25%		214.7	$ 80.00	$ 69.20
LKR	JHK.N0000	John Keells Hold PLC	19.5%	$ 174	$ 159	$ 15	10%		270	$194.25	$191.00
$C	FOM.V	Foran Mining	22.0%	$ 227	$ 218	$ 9	4%		74	$ 4.16	$ 3.90
$C	OLA.TO	Orla Mining	17.6%	$ 210	$ 122	$ 88	72%		55.4	$ 5.13	$ 2.91
$US	BB	Blackberry	8%	$ 126	$ 162	$ (36)	-22%		45.8	$ 2.76	$ 3.54
$US	KW	Kennedy Wilson	10%	$ 114	$ 165	$ (51)	-31%		13.3	$ 8.58	$ 12.38
C$	ALS.TO	Altius Minerals	14%	$ 102	$ 93	$ 8	9%		6.7	$ 20.55	$ 18.44
	MTM - Top 10 Holdings			**$ 2,394**	**$ 2,333**	**$ 60**	**3%**				
	MTM - Smaller Holdings										
$US	GOOG	Alphabet		$ 42	$ 39	$ 3	8%		0.2746	$152.26	$140.93
$C	ESI.TO	Ensign Energy Service	12.9%	$ 42	$ 36	$ 6	17%		21.8	$ 2.59	$ 2.17
$US	CCAP	Crescent Capital		$ 36	$ 36	$ (0)	-1%		2.092	$ 17.26	$ 17.38
$US	BEN	Franklin Resources		$ 28	$ 30	$ (2)	-6%		1.0	$ 28.11	$ 29.79
$US	MRK	Merck		$ 23	$ 19	$ 4	21%		0.1729	$131.95	$109.02
$US	BABA	AliBaba		$ 21	$ 23	$ (2)	-7%		0.2928	$ 72.36	$ 77.51
$US	HP	Helmerich & Payne		$ 23	$ 20	$ 3	16%		0.55511	$ 42.06	$ 36.22
$US	VOO	Vanguard Index 500		$ 19	$ 17	$ 2	10%		0.04	$480.70	$436.80
$US	BNS	Bank of Nova Scotia		$ 15	$ 14	$ 1	6%		0.289	$ 51.78	$ 48.69
$US	GM	General Motors		$ 17	$ 14	$ 4	26%		0.37597	$ 45.35	$ 35.92
$US	JNJ	Johnson and Johnson		$ 12	$ 12	$ 0	1%		0.0734	$158.19	$156.74
$US	TSM	Taiwan Semi		$ 13	$ 10	$ 3	31%		0.0937	$136.05	$104.00
$US	PFE	Pfizer		$ 13	$ 13	$ (0)	-4%		0.46	$ 27.75	$ 28.79
$US	INTC	Intel		$ 8	$ 11	$ (3)	-25%		0.19	$ 44.17	$ 59.25
	Remaining Smaller Holdings			$ 2,199	$ 2,199						
	Total Smaller Holdings			**$ 2,511**	**$ 2,492**	**$ 19**	**1%**				
	Total Mark To Market (Top 10 + Smaller H			**$ 4,905**	**$ 4,825**	**$ 79**	**2%**				
	BDT Capital Partners			$ 683	$ 683	**$ -**	**0%**				
	ShawKwei & Partners			$ 504	$ 504	**$ -**	**0%**				
	JAB Holding Co - JCP V			$ 160	$ 160						
	Other Limited Partnerships			$ 718	$ 718	**$ -**	**0%**				
	Total Limited Partnerships			**$ 2,065**	**$ 2,065**	**$ -**	**0%**				
	Total A: Mark to Market			**$ 6,970**	**$ 6,890**	**$ 79**	**1%**			**$ 3.45**	

Fairfax Financial - Summary of Equity Holdings (Page 2 of 2)

	Yahoo Fin Ticker	Stocks	own %	$ US Market Value Total 31-Mar	Total 31-Dec	Change (mill $)	%	Carrying Value	owned shares (million)	Local Currency 2021 31-Mar	31-Dec
	B.) Associates - Equity Accounted (gains or losses do not flow through financial statements)										
EUR	EUROB.AT	Eurobank	34%	$ 2,436	$ 2,252	$ 184	8.2%	$ 2,099	1,266	€ 1.782	€ 1.610
$US	Private	Poseidon	43%	$ 2,046	$ 2,046			$ 1,706	132		
$US	Private	EXCO Resources	49%	$ 435	$ 435			$ 418	22.9		
$C	STLC.TO	Stelco	24%	$ 429	$ 493	$ (64)	-13%	$ 292	13	$ 44.67	$ 50.19
INR	QUESS.BO	Quess	35%	$ 320	$ 322	$ (1)	-0.4%	$ 430	51.2	₹ 521.4	₹ 522.6
$US	Private	Kennedy Wilson Partnerships		$ 143	$ 143			$ 143			
$US	Private	Peak Achievement	43%	$ 226	$ 226			$ 129			
$US	HFPC-U.TO	Helios Fairfax Partner	36%	$ 101	$ 95	$ 6	6%	$ 198	37.3	$ 2.71	$ 2.55
PLN	AST.WA	Astarta Holdings NV	30%	$ 55	$ 55	$ (0)	-0.3%		7.5	$ 28.90	$ 28.70
PLN	OVO.WA	Ovostar Union PLC	27.5%	$ 28	$ 30	$ (3)	-8.5%		1.65	$ 67.00	$ 72.50
INR	IIFLSEC.BO	IIFL - Securities	3.38%	$ 15	$ 18	$ (3)	-16.5%		10.3	₹ 122.7	₹ 146.7
		Other Associates		$ 697	$ 697			$ 793			
	Total B: Associates - Equity Accounted			**$ 6,931**	**$ 6,812**	**$ 119**	**2%**	**$ 6,208**		**$ 5.17**	
									FV vs CV	**$ 722**	**$31.40**
	C.) Consolidated Equities (gains or losses do not flow through financial statements)										
$US	FIH-U.TO	Fairfax India	43%	$ 860	$ 876	$ (16)	-1.8%	$ 758	57.6	$ 14.93	$ 15.20
C$	Private	Recipe	84%	$ 684	$ 684			$ 684	49.4		
INR	THOMASC(	Thomas Cook India	65%	$ 599	$ 491	$ 108	22.0%	$ 201	300.3	$166.35	$136.15
	Private	Grivalia Hospitality	85%	$ 567	$ 567			$ 567			
C$	DXT.TO	Dexterra / Horizon Nc	49%	$ 130	$ 138	$ (8)	-5.8%	$ 109	31.8	$ 5.55	$ 5.76
C$	BRMI.TO	Boat Rocker	45%	$ 17	$ 25	$ (8)	-32%	$ 84	25.3	$ 0.90	$ 1.30
	Private	Sporting Life	88.5%	$ 62	$ 62			$ 62			
$US		Other Consolidated		$ 29	$ 29			$ -			
	Total C: Consolidated Equities			**$ 2,949**	**$ 2,872**	**$ 76**	**3%**	**$ 2,465**		**$ 3.32**	
									FV vs CV	**$ 484**	**$21.03**
	Total: A + B + C			**$16,849**	**$16,574**	**$ 275**	**1.7%**				
	D.) Other Holdings: Total Return Swaps										
$US	FRFHF	Fairfax Total Return Swaps		$ 2,119	$ 1,809	$ 311			1.964	$ 1,079	$920.76
	Total D: Other			**$ 2,119**	**$ 1,809**	**$ 311**				**$ 13.52**	
	Total A + B + C + D			**$18,968**	**$18,383**	**$ 585**	**3.2%**			**$ 25.45**	

	E.) Other Holdings: Warrants + Debentures Etc										
EUR	MYTIL.AT	Mytilineos Exchang B(	6.4%	$ 97	$ 101	$ (5)	-5%		2.5	$ 35.76	$ 36.70
$US	KW	Kennedy Wilson Warrants		$ 300	$ 300	$ -			13	$ 23.00	$ 23.00
$US	KW	Kennedy Wilson Warrants		$ 200	$ 200	$ -			12.3	$ 16.33	$ 16.33
$US	HFPC-U.TO	Helios Fairfax Partners		$ 100	$ 100	$ -	0.0%		3	$ 4.90	$ 4.90
GBP	DUKE.LON	Duke Royalty Ltd warrants		$ -	$ -	$ -			41.6	$ 0.45	$ 0.45
LKR	JHK.N0000	John Keells Hold PLC	13.0%	$ 63	$ 58	$ 6			98.1	$194.25	$191.00
	Total D: Other			**$ 760**	**$ 759**	**$ 1**				**$ 0.03**	

Equity Holdings – Size Ranking at March 31, 2024

March 31, 2024

Fairfax has an total investment portfolio of about $67 billion, with the split roughly as follows:

Fairfax Estimated Investment Portfolio		
March 8, 2024	$bn	Split
Fixed Income	$45	67%
Preferred Stocks / Property	$3	4%
Equities / TRS	$19	28%
Total Investments	**$67**	

In this post we review the holdings in the equities bucket. To value a holding, we normally use current market value, which is the stock price at March 31, 2024, multiplied by the number of shares Fairfax owns. For private holdings we use Fairfax's latest reported market/carrying value, which was Dec 31, 2023. Derivative holdings, like the FFH-TRS, are included at their notional value.

Additional notes:

1. Mytilineos *: includes exchangeable bonds
2. John Keells *: includes convertible debentures

What holdings are missing from my list below? AGT Food Ingredients and new purchase Meadow Foods (2023) are two that come to mind. I just have no idea what they are worth.

Ok, let's get to the fun part of this post.

What are some of the key take-aways?

1.) Fairfax has a pretty concentrated portfolio

- The top 3 holdings make up 34.5% of the total
- The top 10 holdings make up 57.3% of the total

2.) Steady improvement in quality of the top holdings over the past 6 years: What happened?

- New money has been invested at Fairfax very well (FFH-TRS, buying more of existing holdings)
- Some high quality businesses have continued to execute well (Fairfax India, Stelco)
- Some businesses, after years of effort, have turned around (Eurobank).
- Some businesses that were severely affected by Covid have emerged stronger (Thomas Cook India, BIAL)
- Some businesses were restructured/taken private (Exco, AGT) and are now performing much better.
- Some low quality businesses were sold/merged/wound down (Resolute Forest Products, APR, Fairfax Africa).
- Some low quality businesses have shrunk in size due to poor results (BlackBerry, Farmers Edge, Boat Rocker).

The important point is the overall quality of Fairfax's largest holdings have been slowly increasing. This should result in higher overall returns from the equity portfolio in the coming years.

3.) What rate of return should this collection of equity holdings be able to deliver in 2024?

- 15% return x $19 billion = $2.85 billion
    - share of profit of associates $1.03 billion
    - dividends $170 million
    - 'other' non-insurance consolidated co's $150 million
    - Net gains on investment $1 billion
    - One-time gains $300 million
    - for associate holdings, change in excess of carrying value to market value $200

This looks like a reasonable target for 2024, looking at the solid prospects/earnings profiles of the current holdings.

4.) A slow shift away from mark-to-market holdings. Today, less than 50% of the total portfolio is held in the mark-to-market bucket. Back in 2019, my guess was closer to 80% of the total portfolio was held in the mark-to-market bucket.

- This shift should have the effect of smoothing Fairfax's reported results moving forward, especially during bear markets. As a reminder, in Q1, 2020, Fairfax had $1.1 billion in unrealized losses (when the equity portfolio was much smaller). As more holdings shift to the 'Associates' and 'Consolidated' buckets, it is the trend in underlying earnings at the individual holdings that will matter to Fairfax's reported results and not a stock price - earnings are much more consistent than a stock price. Lower volatility in reported earnings should help Fairfax's valuation (as volatility is considered bad by Mr. Market).
- This shift will also start to create a Berkshire Hathaway problem for Fairfax: over time book value will become an increasingly poor tool to use to value Fairfax. Why? The value of the 'Associates' and 'Consolidated' companies captured in book value each year will fall short of the increase in their true economic value. Fairfax India is a good example of this today. Eurobank is a holding to watch moving forward.

Bottom line, Fairfax looks very well positioned today. But the story gets better: like the past 6 years, I expect the quality of Fairfax's equity holdings to continue to improve in 2024. That will improve future returns. And, like a virtuous circle, the growing cash flows will be re-invested growing the companies even more.

Fairfax - Equity Holdings Ranked by Size			Estimated				
March 31, 2024 (US$ millions)			Market			Ownership	
Rank	Ticker	Holding	Value	Weight		%	Shares
1	EUROB.AT	Eurobank	$2,436	12.7%		34%	1,266
2	FRFHF	Fairfax - TRSwaps	$2,119	11.1%	Top 3		1.964
3	Private	Poseidon	$2,046	10.7%	34.5%	43%	132
4	FIH-U.TO	Fairfax India	$860	4.5%		43%	57.6
5	Private	Recipe	$684	3.6%		84%	49.4
6	Private	BDT Capital Partners	$683	3.6%			
7	THOMASC(	Thomas Cook India	$599	3.1%		65%	300.3
8	Private	Grivalia Hospitality	$567	3.0%		85%	
9	Private	ShawKwei & Partners	$504	2.6%	Top 10		
10	MU	Micron Tech	$461	2.4%	57.3%	0.7%	3.912
11	Private	EXCO Resources	$435	2.3%		49%	22.9
12	STLC.TO	Stelco	$429	2.2%		24%	13
13	EGS60121(	Com Int Bank - Egypt	$362	1.9%		7%	214.7
14	OXY	Occidental Petroleum	$357	1.9%		1.0%	5.5
15	MYTIL.AT	Mytilineos *	$355	1.9%		6.7%	6.7
16	QUESS.BO	Quess	$320	1.7%		35%	51.2
17	JHK.N0000	John Keells *	$237	1.2%		19.5%	270
18	FOM.V	Foran Mining	$227	1.2%		22.0%	74
19	Private	Peak Achievement	$226	1.2%	Top 20	43%	
20	OLA.TO	Orla Mining	$210	1.1%	73.8%	17.6%	55.4
21	Private	JAB Holding Co - JCP V	$160	0.8%			
22	Private	Kennedy Wilson Partner	$143	0.7%			
23	DXT.TO	Dexterra	$130	0.7%		49%	31.8
24	BB	Blackberry	$126	0.7%		8%	45.8
25	KW	Kennedy Wilson	$114	0.6%		10%	13.3
26	ALS.TO	Altius Minerals	$102	0.5%		14%	6.7
27	HFPC-U.TO	Helios Fairfax Partners	$101	0.5%		36%	37.3
28	Private	Sporting Life	$62	0.3%		88.5%	
29	AST.WA	Astarta Holdings NV	$55	0.3%	Top 30	30%	7.5
30	GOOG	Alphabet	$42	0.2%	79.2%		0.275
		Remainder	$3,973	20.8%			
		Total	**$19,127**				
	Private	Private holdings: market value at Dec 31, 2023					
	* Includes exchangeable bonds / convertible debentures						
	Holdings missing from list? AGT Food Ingredients and Meadow Foods.						

A Review of Fairfax's Commodity Holdings

Updated December 31, 2023

Fairfax has certainly hit the ball out of the park with its commodity holdings over the past couple of years. Selling Resolute Forest Products in 2022 at the top of the lumber cycle at a premium valuation was certainly well done. The value of the various commodity holdings currently total around $1.8 billion = 10% of total equity holdings of about $18 billion. The holdings are very diversified and look well positioned to deliver solid value to Fairfax in the coming years.

- Stelco ($493 million): this has turned into a great investment. Given all the share buybacks done by Stelco, Fairfax has ownership stake increase from 14% to almost 24% over the past 18 months. And Kestenbaum is still sitting on a significant amount of cash. Another great asset to own. Steel looks poised to do well as we get to the other side of the economy in another year or so. With Fairfax now owning more than 20%, this is now an associate/equity accounted holding.

- Foran Mining ($211 million): Fairfax owns 21% of Foran, which is developing a copper mine in Canada that could begin production in a couple of years right when sales of EV's are taking off… and a shortage of copper develops. Most analysts are forecasting much higher prices for copper looking out a couple of years. This investment will be one to watch moving forward as it has the potential to be another big winner for Fairfax.

- Altius Minerals ($93 million): Fairfax owns 14% of this diversified royalty company with exposure to potash, iron, copper etc. Quality company… chug, chug, chug.

- Orla Mining ($110 million). Fairfax has been adding to this position over the past year.

Fairfax also has a sizeable exposure to energy:

- Exco ($545 fair value). Exco is a natural gas producer.

- Occidental Petroleum ($359 million); Fairfax materially added to this position in 2023.

- Ensign Energy Services ($36 million): Fairfax owns 13% of this oil and gas services company. Looks well positioned.

Chapter 10: Investments – Equities – History Lessons

Fairfax has three economic engines:

1. Insurance
2. Investments – fixed income
3. Investments – equities

Chapter 10 will review some of the history of Fairfax's third engine: Investments – equities. This is important because the underperformance of Fairfax from 2010 to 2020 was primarily due to significant mistakes made by the company with holdings in this bucket. As those mistakes were corrected the financial performance of the company improved markedly.

A Review of 2018-2022: New Fairfax

April 15, 2023

Why 'new Fairfax?' My view is something changed at Fairfax around 2018 in how they were managing the equity side of their investment portfolio. Around that time, they appeared to put more of a premium on investing in companies with strong management – Hamblin Watsa was not a turn-around shop. The companies also needed to be in good financial shape and able to fund their growth ambitions on their own. Fairfax was no longer going to be a piggy bank for poorly run, struggling companies.

This post will review ten of Fairfax's largest equity purchases made from 2018 to today. As a group, these investments have already delivered considerable value to Fairfax shareholders. And they look well positioned for the future.

1.) <u>Fairfax Total Return Swap (TRS)</u> - equity derivative (2020): Late in 2020 and early in 2021, Fairfax purchased TRS giving it exposure to 1.96 million Fairfax shares at an average cost of $372.96/share. Fairfax shares closed Friday at $658/share. This puts the gain at $285/share (+71%) = $559 million (before cost to carry TRS).

That is an exceptional return over 28 months. Fairfax shares, trading at 1 x trailing BV, still look cheap. This investment could deliver another $250 million return to Fairfax shareholders in each of the next 2 years. If this happens, this will put the total return at over $1 billion. This investment is quickly becoming one of Fairfax's best.

2.) Fairfax 'dutch auction' stock buyback (2021): in the fall of 2021, Fairfax made another investment in Fairfax, buying 2 million shares at $500/share, for a total of $1 billion. Fairfax's book value at Dec 31, 2022 was $658/share. My guess is book value on Dec 31, 2023 will be about $770/share. Stock buybacks should only be done when your shares are trading at a discount to intrinsic value. This investment looks very good for shareholders.

These first two investments show Fairfax at its very best. Value investors. Opportunistic. Creative. Aggressive (with position size). Timed perfectly.

3.) Seaspan (2018 & 2019): In February 2018, Fairfax made their first investment in Seaspan (now Atlas). Why? David Sokol. Atlas is Fairfax's largest equity holding today. Fairfax owns 131 million shares of Atlas (43%) with a carrying value of $1.5 billion ($12.39/share) and a market value of $1.865 billion ($15.34/share). The first 76 million shares were purchased by Fairfax at $6.50/share.

In the 2022AR, Prem said as the new-build strategy is executed Atlas may hit EBITDA of $1.75 billion in 2025; in 2022 adjusted EBITDA was $1.135 billion. In 2022 Atlas delivered share of profit of associates of $258 million to Fairfax. This number looks likely to increase in the coming years. This investment looks poised to be another $1 billion winner for Fairfax.

4.) Stelco (2018): in late 2018, Fairfax invested $193 million for a 13.7% stake in Stelco. A steel producer? At the time I did not like the purchase. It screamed 'old Fairfax' to me. Boy, was I wrong. Steel went to record prices. The CEO, Alan Kestenbaum, is exceptional. Stelco has paid regular and large special dividends. Fairfax's position is now worth $470 million, and they own 23.6% of Stelco. This investment has performed exceptionally well for Fairfax shareholders. Steel looks to be in a secular bull market – with all the infrastructure/energy transition/home-shoring plans.

5.) Foran Mining (2021): in Aug 2021, Fairfax invested $78 million in Foran Mining. Pierre Lassonde is another large shareholder (founder of Franco-Nevada). Foran is developing a large copper mine in Saskatchewan. As we execute the EV transition, looking out only a couple of years, it is expected demand for copper could exceed its supply. Right about the time when this mine should be starting up production. Market value of Fairfax's position is currently $220 million. If the mine works out, and copper prices move much higher, this investment could go much higher. Yes, lots of risk.

6.) Recipe (2022): in August 2022, Fairfax invested $342 million (with $100 million coming from Recipe itself) to take Recipe private. Fairfax now owns 84%. Fairfax has been a major consolidator of the Canadian restaurant industry starting in 2012. They understand Recipe very well. They got the asset at an attractive price (at a Covid discount). Recipe has a carrying value of $594 million for Fairfax. Recipe generated free cash flow of about $110 million each year from 2017-2019 (pre-Covid). They should be able to get back there, which would deliver about $95 million/year to Fairfax. This could become a meaningful and predictable cash generator for Fairfax moving forward.

7.) Large cap stocks (BAC, OXY, CVX, MU): In Q2 and Q3 of 2022, Fairfax invested $380 million in US large cap stocks. Banking. Energy. Technology. Solid companies. Good core, long-term holdings that should deliver a solid return for Fairfax shareholders in the years to come.

8.) Grivalia Hospitality (2022): in July 2022, Fairfax increased their stake in Grivalia Hospitality – purchased from Eurobank for $195 million. Here is what Prem had to say in the 2022AR: "Recognizing the outstanding results achieved at Grivalia Hospitality by George Chryssikos, Vice

Chair of Eurobank, in 2022 we increased our ownership to 78%. Grivalia Hospitality is a leading investor in Greece's booming ultra- luxury hotel space, with three operating assets and seven under development. You will remember that George ran Grivalia Properties, a public company of which we owned 51%. Eurobank and Grivalia Properties merged in 2019 when Eurobank needed capital. The gains from Grivalia Properties and the Eurobank shares we acquired on the merger have resulted in a total gain to Fairfax of approximately $1 billion. We gratefully add George's name to Richie Boucher's from the Bank of Ireland, who was our first billion dollar man." Fairfax has done exceptionally well investing alongside of George Chryssikos. Let's hope George's Midas touch continues to the benefit of Fairfax shareholders.

9.) <u>Dexterra/Carillion/Horizon North (2018)</u>: in March of 2018, Fairfax purchased Carillion Canada out of bankruptcy protection (it was the UK operations that were in trouble). In May of 2020, Dexterra engineered a reverse takeover of Horizon North. Fairfax owns 49% of Dexterra. The company has a near-term target to get to C$100 million in EBITDA. They are funding their growth internally. 2022 had some near-term challenges (inflation and labour) in Modular Solutions and IFM units. Carrying value is $103 million. Market value today is $121 million. There is a good chance company could get to its C$100 million EBITDA target in the next couple of years.

10.) <u>Toys "R" US (2018)</u>: In 2018, Fairfax purchased Toys "R" Us Canada out of bankruptcy for $235 million. At the time of purchase this transaction was a bit of a head scratcher. However, in 2021, Fairfax sold the retail operations and kept the real estate, and the transaction made much more sense. Not sure what the current value is.

A Review of 2014 to 2017: Old Fairfax

April 14, 2023

Fairfax's equity portfolio looks very well positioned today. Most of the equity holdings purchased since 2018 have been performing well. And, after years of hard work, the poor performing equity holdings (many purchased from 2014-2017) have largely been fixed and are now performing well. In fact, the equity portfolio looks better positioned today than at any other time in Fairfax's recent history. We are increasingly seeing the benefits in improved reported results. A good recent example is 'share of profit of associates,' which spiked to more than $1 billion in 2022; the previous high was $402 million in 2021.

<u>What happened?</u> Three things:

1.) Fairfax learned a few important lessons from the poor purchases they made from 2014-2017. It looks me like Fairfax has tweaked the methodologies used when allocating capital.

- They are putting a premium on management. Hamblin Watsa has decided it is not a turn-around shop - looking to actively run poorly lead/challenged businesses.

- They are also looking to invest in better balance sheets. Fairfax is no longer a piggy bank for poorly run companies in search of cash. Others on this board have pointed this out.

2.) the Fed and the ending of easy money (zero interest rates/QE) is likely a driver of the stronger performance the past two years of Fairfax's equity holdings. Value investing is back.

3.) the timing of the cycle is finally working in Fairfax's favour and is driving stronger performance of the equity holdings. Value, resource, and commodity stocks appear to be in a secular bull market.

At the end of the day, all the above is likely partly responsible for the improvement we have seen in Fairfax's equity holdings in recent years.

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It can be instructive to look into the past so we can learn. This helps us understand what has been baked into past results. In turn, this can help us understand what might happen in the future.

<u>What happened with the purchases from 2014-2017?</u>

A total of 10 investments are reviewed below. Fairfax invested a total of about $3.5 billion in these investments over the years. Over the past 8 years my math says Fairfax booked losses of about $1.5 billion on these holdings. That is almost $200 million, on average, each year. For example, in 2022, Fairfax wrote down its investment in Farmers Edge by $133 million. Stuff like that.

The bigger cost to shareholders has been the opportunity cost. Prem tells us that Fairfax expects its equity investments to deliver returns of 15% per year. Applying a more modest 10% target, the $3.5 billion in investments (made 2014-2017) should have doubled in value by now to $7 billion. The opportunity cost of the poor investments made from 2014-2017 is likely an additional $2 billion.

This is actually a good news post. The good news is:

1. The equity purchases made from 2018 to April 2023, as a group, look very good and are performing well.
2. As I will review below, the problem investments from 2014-2017 look like they are not only fixed - they are also poised to deliver solid returns for Fairfax shareholders moving forward. An 8 year-long headwind has now become a tailwind.

As a result, I expect Fairfax's $16 billion equity portfolio to generate a higher total return (percent and absolute) in the coming years than it has delivered over the last decade. Given its current construction, it could well compound at 12% over the next couple of years = $1.9 billion/year:

- dividends = $120 million
- share of profit of associates = $900 million
- consolidated earnings = $240 million
- mark-to-market investment gains = $650 million (not including fixed income)

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Below is a short review of 10 large investments made over the 4 years from 2014-2017.

1.) EXCO Resources (2015): Fairfax's initial investment was $300 million in 2015. We have since learned that shale was a bubble and it eviscerated something like $5 billion in capital up until 2020. Fairfax reported cumulative realized losses of $296 million on EXCO in 2019 (as per the AR).

- Learning: the old economic model for shale was a sham.
- The good news: energy looks like it is in a structural bull market; the new economic model for shale looks good - focussed on shareholder return.

2.) APR (2016): Fairfax invested a total of $462 million in APR in 2016 and 2017. In 2018 they sold it to Atlas for $200 million (in Atlas stock). The first thing Atlas did was replace the CEO.

- Learning: Terrible business. Poorly managed.
- The good news: APR is now Atlas' problem.

3.) Fairfax Africa (2017): launched with much fanfare in 2017, Fairfax invested a total $476 million. Two short years later Fairfax exited its management of the business and moved the assets to a fund managed by Helios. The value of the Helios fund today is about $100 million. I am not sure what the total financial loss was for Fairfax on this investment, but it was significant. The damage to Fairfax's reputation was also significant.

- Learning: Hubris on steroids? Terrible idea. Worse execution.
- The good news: Fairfax is partnered with Helios and looks well positioned moving forward in Africa. This is now a small investment for Fairfax.

4.) Farmers Edge (2017): Fairfax invested $159 million in Farmers Edge in 2017. Farmers Edge completed its IPO in 2021 and in the 2021 AR Fairfax said their total investment in Farmers Edge to that point was $376 million. The CEO 'stepped down' in April of 2022. In the 2022 AR, Fairfax said Farmer's Edge had a carrying value of $71 million, after taking a $133 million write down in 2022. The market value of Fairfax stake was $5 million at Dec 31, 2022. My guess is this investment, because it performed so terribly post-IPO, has caused Fairfax some damage to its reputation (given Fairfax was the majority shareholder).

- Learning: Yup, SPAC's were a bubble.
- The good news: carrying value is $71 million. This is now a small investment for Fairfax.

5.) Eurobank (2014): Fairfax invested $444 million in Eurobank in 2014. This initial investment went to close to zero later that year when the ECB mandated a 1-for-100 reverse share split. What was the problem? Greece was in the midst of a depression. What did Fairfax do? It doubled down and invested another $389 million in Eurobank in 2015. In 2019, Eurobank did a capital raise/merger with Grivalia. Greece elected a pro-business government in 2018. Eurobank fixed its balance sheet.

- Learning: Because the strategy worked in Ireland doesn't mean it would work in Greece.
- The good news: Greece's economy is well positioned. Eurobank, always well managed, is executing well and earnings are spiking. Share of profit of associates was $263 million in 2022, up from $162 million in 2021. Prem estimated Eurobank could earn €0.20/share in 2023; if so, Fairfax's share of profits for Eurobank could be +$300 million in 2023. This investment is turning into a home run for Fairfax - a Greek tragedy turns to a triumph!

6.) AGT (2017): Fairfax invested $148 million in AGT in 2017. In 2019, as AGT was experiencing financial difficulties, Fairfax took AGT private, spending another $227 million (I think).

- Learning: It takes much more than a dynamic Canadian founder to succeed.

- The good news: from 2022 Fairfax AR: "AGT, run by founder and CEO Murad Al-Katib, had a record year in 2022, with EBITDA of over Cdn$150 million. This is a dramatic improvement from the time of the take-private transaction almost four years ago when the business was generating slightly over Cdn$60 million in EBITDA… Fairfax has an approximate 60% stake in AGT."

7.) Commercial Industrial Bank (CIB) Egypt (2014): Fairfax invested $330 million in CIB in 2014. Today the position is worth about $240 million. Great company. Solid management. What is the problem? Egypt's economy has been a slow-moving train wreck for decades - with constant currency devaluations.

- Learning: Constant currency devaluations (like 50% in the last year) hurt equity values.
- The good news: the bank is well managed.

8.) Mosaic Capital (2017): Fairfax invested $116 million in Mosaic in 2017. In 2021, Mosaic was taken private (not by Fairfax) with Fairfax owning 20% of the new investment. This investment went sideways for many years (that opportunity cost thing).

- Learning: not every investment you make is going to work out.
- The good news: Fairfax found a partner where Mosaic will hopefully be a better fit.

9.) Recipe/CARA (2014 & 2016): Fairfax made a couple of restaurant investments from 2014-2017: $77 million in the Keg in 2014 (merged with CARA in 2018) and $100 million in the CARA capital raise in $2016. Recipe/CARA was a poor investment for minority shareholders over its lifetime.

- Learning: the restaurant business in Canada is a tough business. Consolidating it proved to be even tougher.
- The good news: In the take private deal in 2022, Fairfax purchased Recipe at a Covid-low price. Recipe has a solid collection of assets that should be able to produce a solid amount of free cash flow for Fairfax moving forward.

10.) Astarta (2017): Fairfax invested $104 million in Astarta in 2017. Today that investment is worth around $45 million. I know very little about this investment. I wonder if it is not a similar situation to CIB, with opportunity cost being the big issue.

Honorable mention: Torstar was initiated as a position before 2014 so I did not include it. However, Fairfax added to its position in 2014, 2016 and 2017 (yes, small amounts). In 2020 it sold the business and booked a $52 million loss.

I see lots of self-inflicted wounds in the investments listed above – reading the list reminds me of the Monty Python skit "tis but a scratch".

Some of Fairfax's Larger Investments Initiated 2014-2018

		cost	
2014	CIB (Egypt)	$330	
	Eurobank	$444	initial investment went to zero
	Keg (CARA)	$77	later folded into CARA
2015	Fairfax India	$300	initial capital raise
	EXCO Resources	$300	
	Eurobank #2	$389	capital infusion
2016	APR	$340	
	CARA	$100	capital raise
2017	Fairfax India #2	$145	second capital raise
	Mosaic	$116	
	Fairfax Africa	$325	initial capital raise
	Farmers Edge	$159	
	Astarta	$104	
	APR #2 & #3	$122	
	AGT Food	$148	
2018	Fair Africa #2	$151	second capital raise
2019	AGT #2	$227	take private
	EXCO		bankruptcy restruc. $296 mill losses
	Eurobank/Grivalia		capital raise / merger
	APR		sale to Atlas for $200 million
	Helios Fairfax		sale/merger to Helios
2021	Mosaic Cap		take private
2022	Farmers Edge		write-down of position - $133
	Total	**$3,777**	

Equity Hedges and Shorts 2010-2020: The Lost Decade

June 10, 2023

> "Those who cannot remember the past are condemned to repeat it." (George Santayana)

Given it has come up in lots of discussions, I thought it would be useful to review what has to be Fairfax's biggest ever investment mistake: the equity hedges and shorts from 2010-2020.

Why are they Fairfax's biggest investment mistake?

The 'equity hedges' were in place from 2010 to 2016… and they caused investment losses of $4.4 billion; an average loss of $628 million per year for 7 straight years.

Shareholders equity in 2010 was $7.7 billion. So, losing $628 million in ONE YEAR was a big deal. And, as a reminder, this happened, on average, for 7 straight years. Book value per share was $376 in 2010 and in 2016 it has fallen to $367. Yes, Fairfax did pay a $10/share dividend every year so shareholders did earn a positive return over these years.

Cumulative Losses Equity Hedges/Shorts		
2010	-$937	equity hedges
2011	$414	equity hedges
2012	-$1,006	equity hedges
2013	-$1,982	equity hedges
2014	-$195	equity hedges
2015	$502	euity hedges
2016	-$1,192	equity hedges/shorts
2017	-$418	short exposure
2018	-$38	short exposure
2019	-$58	short exposure
2020	-$529	short exposure
2010-2016	**-$4,396**	**Total**
2010-2016	-$628	Average
2010-2020	**-$5,438**	**Total**
2010-2020	-$494	Average

Why did Fairfax put on the equity hedge trade?

Back in 2010, Fairfax was afraid "the North American economy may experience a time period like the U.S. in the 1930s and Japan since 1990."

"2010 was a disappointing year for HWIC's investment results because of the two factors mentioned earlier. Hedging our common stock investment portfolio cost us $936.6 million or $45.61 per share in 2010. Our hedging program masked the excellent common stock returns we earned in 2010, of which a significant amount was realized ($522.1 million). We began 2010 with about 30% of our common stock hedged. In May and June, we decided to increase our hedge to approximately 100%. Our view was twofold: our capital had benefitted greatly from our common stock portfolio and we wanted to protect our gains, and we worried about the unintended consequences of too much debt in the system – worldwide! If the 2008/2009 recession was like any other recession that the U.S. has experienced in the past 50 years, we would not be hedging today. However, we worry, as we have mentioned to you many times in the past, that the North American economy may experience a time period like the U.S. in the 1930s and Japan since 1990, during which nominal GNP remains flat for 10 to 20 years with many bouts of deflation." Prem Watsa – Fairfax 2010AR

Why did Fairfax exit the equity hedge trade?

The US presidential election on November 8, 2016.

"Unfortunately, the presidential election on November 8, 2016 changed the world for us, so we reacted quickly by removing all our index hedges and some of our individual short positions and reducing the duration of our fixed income portfolios to approximately one year – all of which resulted in a $1.2 billion net loss on our investments in 2016 which, in turn, resulted in a loss in 2016 of $512 million or $24.18 per share." *Prem Watsa – Fairfax 2016AR*

But our sad story does not end here because even though Fairfax exited all of their equity hedge positions late in 2016, they continued with some individual company short positions. From 2017-2019, Fairfax lost another $514 million on short positions.

"In the past, to protect our equity exposures in uncertain times, we shorted indices (mainly the S&P500 and Russell 2000) and a few common stocks. After much thought and discussion, it became clear to me that shorting is dangerous, very short term in nature and anathema to long term value investing. As I mentioned to you in last year's annual report, shorting has cost us, cumulatively, net of our gains on common stock, approximately $2 billion! This will not be repeated! In the future, we may use options with a potential finite loss to hedge our equity exposure, but we will never again indulge anew in shorting with uncapped exposure. Your Chairman continues to learn–slowly!!"

Prem Watsa – Fairfax 2019AR

But even after the mea culpa above in the 2019AR, shareholders learned in 2020 that there was still one last mystery short position on the books. Only after another $529 million in losses in 2020, did Fairfax finally come to the conclusion that shorting was a tricky business. Margin and unlimited losses can be a bitch, especially in a decade long bull market (S&P500 was 1,133 on Jan 1, 2010 and 3,756 on Dec 31, 2020).

And there we have it: Fairfax's lost decade for shareholders from 2010-2020.

"I said in our 2019 annual report that we would not short stock market indices (like the S&P500) or common stocks of individual companies ever again, and our last remaining short position was closed out in 2020 (not soon enough, as it cost us $529 million in 2020)." *Prem Watsa – Fairfax 2020AR*

So, beginning in 2021, Fairfax shareholders were finally able to close the book on the whole 'equity hedge/short' trades.

<u>What was the cost to Fairfax?</u>

- Investment losses of $5.4 billion from 2010-2020, or $494 million per year on average.
- Additional significant opportunity cost - easily in the billions.
- The massive size of the losses each year likely warped capital allocation decisions, especially from 2010-2016, when the losses were larger.
- Long lasting harm to Fairfax's reputation in the investment community.
- Exit of many long-term shareholders.

<u>What went wrong?</u>

The size and duration of the position. The losses were massive. And they were allowed to go on (pretty much) for 11 straight years.

<u>What explains the mistake?</u>

No idea. But my guess is hubris. Fairfax had just made billions from 2007-2009 with their credit default spread (CDS) and equity hedge positions (this is discussed in the next post titled 'Credit Default Swaps 2005-2009: The Big Short – Fairfax Edition). That spectacular win likely laid the groundwork for their subsequent spectacular fall.

<u>Hubris Comes From Ancient Greece</u>

"English picked up both the concept of hubris and the term for that particular brand of cockiness from the ancient Greeks, who considered hubris a dangerous character flaw capable of provoking the wrath of the gods. In classical Greek tragedy, hubris was often a fatal shortcoming that brought about the fall of the tragic hero. Typically, overconfidence led the hero to attempt to overstep the boundaries of human limitations and assume a godlike status, and the gods inevitably humbled the offender with a sharp reminder of their mortality." *Merriam-Webster*

<u>Will Fairfax make the same mistake again?</u>

Well, this is where things get interesting. Fairfax has stated publicly numerous times that they won't make that <u>exact same mistake</u> again. To the best of my knowledge, they have never discussed publicly the failures with their internal processes that allowed such a flawed investment to be made (in such a large size and for such a long duration). Did they identify the internal failures? Have they made the internal changes necessary to ensure **it** (a terrible investment decisions that results in another lost decade for shareholders) does not happen again? I'm not sure…

Summary:

As shareholders, I think it is important that we discuss/remember not only Fairfax's successes but also their failures. I call it 'eyes wide open'. The equity hedges were an unmitigated disaster for Fairfax and its shareholders. There is no way to put lipstick on this pig.

What is missing from my analysis?

The 'equity hedge/short' trade was just one piece in the bigger picture of what Fairfax was doing as a company at the time. Fairfax's decisions are not made in a vacuum. That is perhaps the biggest flaw with my long-form posts… they usually do not include an overlay of other important 'big picture' pieces. Readers need to keep this in mind.

Comments from Prem and other notes from Fairfax's 2016AR.

"Unfortunately, the presidential election on November 8, 2016 changed the world for us, so we reacted quickly by removing all our index hedges and some of our individual short positions and reducing the duration of our fixed income portfolios to approximately one year – all of which resulted in a $1.2 billion net loss on our investments in 2016 which, in turn, resulted in a loss in 2016 of $512 million or $24.18 per share."

"When we removed our hedges near the end of 2016, we realized a loss of $2.6 billion in 2016, but that included $1.6 billion which had gone through our statements in prior years. As discussed earlier, since 2010 we have had $4.4 billion of cumulative net hedging losses and $0.5 billion of unrealized losses on deflation swaps (which we still hold), offset entirely by net gains on stocks of $2.7 billion and net gains on bonds of $2.2 billion. The volatility of our earnings caused by our hedges and long bond portfolios is over – and as I said earlier, we are focused on once again producing excellent investment returns." *Prem Watsa – Fairfax 2016AR*

Equity contracts: "Throughout 2015 and most of 2016, the company had economically hedged its equity and equity-related holdings (comprised of common stocks, convertible preferred stocks, convertible bonds, non-insurance investments in associates and equity-related derivatives) against a potential significant decline in equity markets by way of short positions effected through equity and equity index total return swaps (including short positions in certain equity indexes and individual equities) and equity index put options (S&P 500) as set out in the table below. The company's equity hedges were structured to provide a return that was inverse to changes in the fair values of the indexes and certain individual equities."

"As a result of fundamental changes in the U.S. that may bolster economic growth and business development in the future, the company discontinued its economic equity hedging strategy during the fourth quarter of 2016. Accordingly, the company closed out $6,350.6 notional amount of short positions effected through equity index total return swaps (comprised of Russell 2000, S&P 500 and S&P/TSX 60 short equity index total return swaps). The short equity index total return swaps closed out in 2016 produced a realized loss of $2,665.4 (of which $1,710.2 had been recorded as unrealized losses in prior years). The company continues to maintain short equity and equity index total return swaps for investment purposes, and no longer considers them to be hedges of the company's equity and equity-related holdings. During 2016 the company paid net cash of $915.8 (2015 – received net cash of $303.3) in connection with the closures and reset provisions of its short equity and equity index total return swaps (excluding the impact of collateral requirements)." *Fairfax 2016AR*

Credit Default Swaps 2005-2009: The Big Short – Fairfax Edition

June 19, 2023

Stanley Druckenmiller on position sizing:

"Sizing is 70% to 80% of the equation. Part of the equation is seeing the investment, part of the investment is seeing myself in a good trading rhythm. It's not whether you're right or wrong, it's how much you make when you're right and how much you lose when you're wrong," says Druckenmiller.

"I believe in streaks," he says, "Like in baseball. Sometimes you're seeing the ball, sometimes you're not. And my number one job is to know when I'm hot and when I'm not. When I'm hot, I need to turn the dial straight up. When you're cold the last thing you should do is make big bets to get even. You need to turn yourself down." *Stanley Druckenmiller*

https://moneyweek.com/investments/investment-strategy/605020/stan-druckenmiller-position-size-really-matters#:~:text="Sizing%20is%2070%25%20to%2080,re%20wrong%2C"%20says%20Druckenmiller

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In the book/movie, 'The Big Short', bestselling author Michael Lewis profiles three firms who made a financial killing from the bursting of the US housing bubble in 2008. How did they do it? They bought credit default swaps (CDS) in 2005 and 2006. Lewis describes it as "One of the best trades in Wall Street history."

"It's been called the worst financial crisis in modern times. Certainly, the largest financial disaster in decades in this country, and perhaps the end of an era in American business. In the end, Lewis Ranieri's mortgage-backed security mutated into a monstrosity that collapsed the whole world economy. And none of the experts and leaders or talking heads had a clue it was coming…. But there were some who saw it coming. While the whole world was having a big old party, a few outsiders and weirdos saw what no one else could… These outsiders saw the giant lie at the heart of the economy. And they saw it by doing something the rest of the suckers never thought to do. They looked." *Micheal Lewis – The Big Short*

The three firms profiled in 'The Big Short' were: Scion Asset Management (Dr. Micheal Burry), FrontPoint Partners (Steve Eisman) and Brownfield Capital (Charlie Gellar and Jamie Shipley). A small Canadian P/C insurer could also have been included in Lewis' book as a 4th participant. Yes, Fairfax Financial.

<u>What was the trade?</u>

They bought a financial derivative called a credit default swap.

In 'The Big Short' movie, a large investor in Burry's fund at Scion summed up the trade perfectly: "In other words, we lose millions until something that has never happened before happens?" Burry replied: "That's right."

Comments from Prem about the credit default swap position from Fairfax's 2005AR.

> "Just a brief overview for you on our credit default swaps, which are 5-year to 10-year fixed income derivatives, which fluctuate with credit spreads, that we have purchased from major banks. Here is an example. To purchase a 5-year $100 million credit default swap on a company that sells at a 30 basis point spread over treasuries, one has to invest 150 basis points (30 basis points/year × 5 years), so $1.5 million purchases protection on an underlying $100 million of credit exposure of the chosen company over the next five years. The maximum loss to the purchaser in 5 years is $1.5 million if the credit spread stays at 30 basis points or tightens even further. On the other hand, if the credit spread on this company doubles to 60 basis points, the credit default swap can be worth as much as $3 million, and if the company goes bankrupt, that swap can be worth up to $100 million. We have a diversified list of companies, mainly financial institutions, with respect to which we have paid approximately $250 million to purchase protection on underlying credit exposures. Accounting rules require these credit default swaps to be marked to market (similar to our S&P500 hedges) on a quarterly basis and the resulting valuation adjustment to be treated as a realized gain or loss."
>
> *Prem Watsa – Fairfax 2005AR*

Credit default swap definition:

> "A credit default swap is a financial swap agreement that the seller of the CDS will compensate the buyer in the event of a debt default (by the debtor) or other credit event. That is, the seller of the CDS insures the buyer against some reference asset defaulting. The buyer of the CDS makes a series of payments (the CDS "fee" or "spread") to the seller and, in exchange, may expect to receive a payoff if the asset defaults." *Wikipedia*

A CDS is insurance on 'something'. It offers a big payout (as much as 20 to 1) if that 'something' defaults/goes bust. Burry bought CDS on MBS. Fairfax bought CDS on a variety of financial and insurance companies.

Why did Fairfax do it?

Fairfax bought the credit default swaps as a hedge - to protect the "investment portfolios from a potential (though low probability) financial market disaster."

Comments from Fairfax about the CDS position from the 2005AR.

> "The company has invested approximately $250 in 5-year to 10-year credit default swaps on a number of companies, primarily financial institutions, to provide protection against systemic financial risk arising from financial difficulties these entities could experience in a more difficult financial environment." *Fairfax 2005AR*

When did Fairfax start buying?

Fairfax initiated their CDS position in 2005, investing $250 million. They were in about the same time as Burry (early). How did it go initially? Not very well. Like Burry, Fairfax booked large investment losses the first two years: $101.6 million in 2005, and another $76.4 million in 2006.

In the movie 'The Big Short,' a realtor describes the US housing market in 2006 as follows: "The markets in an itsy-bitsy little gully right now."

But early in 2007, the US housing market began to quickly unravel, and it just kept getting worse from there. Fairfax added to their CDS position in early 2007. During the rest of the year the CDS worm began to turn and by the end of 2007, Fairfax was suddenly sitting on a $1 billion gain. 2008 saw Fairfax book another $1 billion gain. Fairfax sold most of their CDS positions in 2008 and early 2009, locking in sizeable gains.

How much did everyone make over the life of the trade?

- Scion = $2.69 billion
- FrontPoint = around $1 billion
- Brownfield = $50 million ($80 - $30 million initial investment)
- Fairfax = 2.1 billion (original acquisition cost was $318 million).

For perspective, in 2008, common shareholder's equity at Fairfax was only $4.9 billion.

I would love to hear the inside story of what actually happened at Fairfax from 2005-2009. It would make a great documentary. An aspiring Canadian producer should get on it. The story would make a compelling addendum to 'The Big Short' (kind of like the recent documentary on YouTube titled 'Luc Longley and the missing chapter of the Last Dance').

How did Fairfax's share price perform?

Fairfax shareholders were big, big winners. For the 4-year period from 2005 to 2009, Fairfax shares increased 174%. During this same 4-year period, the S&P500 decreased 11%. On a relative basis, from 2005-2009, Fairfax's shares had close to 200% outperformance over the S&P500. I am getting a little déjà vu (of Fairfax outperforming again in a bear market).

Fairfax	Earnings	Book Value	Share Price		S&P 500	
	per share					
2005	-$27.75	$137.50	$143.36		1,248	
2006	$11.92	$150.15	$198.50	38%	1,418	14%
2007	$58.38	$230.01	$286.13	44%	1,468	4%
2008	$79.53	$278.28	$313.41	10%	903	-38%
2009	$43.75	$369.80	$393.00	25%	1,115	23%
4-year change		169%	174%		-11%	

Lots of 'Corner of Berkshire and Fairfax' members made a killing on Fairfax stock over the 4 years from 2006-2009. In mid-2006, Fairfax's stock briefly traded below $100. It traded over $300/share in early 2008.

And a few board members made their own trade of the century: they purchased Fairfax leaps (in 2006?) and made millions (at the time Fairfax was traded on the NYSE so derivatives were available).

What does all this mean for Fairfax today?

Does something that happened around 15 years ago matter all that much today? I am not sure.

Of interest, a few of the people who were deeply involved with the CDS trade are still with the company. However, Fairfax - the company - is a completely different animal today. Most importantly, its insurance business is much larger and of much higher quality. Its bond portfolio is positioned perfectly. And its equity portfolio is high quality. As a result, Fairfax is generating record underwriting profit, record interest and dividend income, record share of profit of associates and solid investment gains - in short, the quality of the earnings stream Fairfax is generating today has never been better, and it appears durable.

What is missing from my analysis?

The CDS trade was just one piece in the bigger picture of what Fairfax was doing at the time. Over the same time period, Fairfax also had significant equity hedges on (this time it worked). And in 2006, the dirty and viscous short campaign against Fairfax reached its climax (driving the stock briefly below $100 in June of that year). Not spending more time on 'the bigger picture' is perhaps the biggest flaw with my long-form posts. Readers need to keep this in mind.

Final summary from Prem on the credit default swap position from Fairfax's 2009AR.

For the last time, we include the table on our credit default swap positions and their disposition.

	Notional Amount	Original Acquisition Cost	Sale Proceeds	Excess of Sale Proceeds Over Original Acquisition Cost
FY 2007	965.5	25.7	199.3	173.6
FY 2008	11,629.8	245.8	2,048.7	1,802.9
Q1 2009	2,902.6	45.5	223.0	177.5
Q2 2009	140.3	1.4	8.6	7.2
Q3 2009	–	–	–	–
Q4 2009	–	–	–	–
Cumulative sales since inception	15,638.2	318.4	2,479.6	2,161.2
Remaining credit default swap positions at December 31, 2009	5,926.2	114.8	71.6(1)	(43.2)(2)
Cumulative realized and unrealized from inception	21,564.4	433.2	2,551.2	2,118.0

(1) Market value as of December 31, 2009

(2) Unrealized loss (measured using original acquisition cost) as of December 31, 2009

In total, since inception we have sold $15.6 billion notional amount of credit default swaps, with an original acquisition cost of $318 million, for cash proceeds of $2.5 billion and a cumulative gain (against original cost) of $2.2 billion. As of December 31, 2009, the remaining $5.9 billion notional amount of credit default swaps had a market value of $72 million against an original acquisition cost of $115 million, an unrealized loss of $43 million. If the remaining credit default swaps all went to zero, our shareholders' capital would be reduced by $72 million pre-tax. Our adventure with credit default swaps is over – but we will remember it as of one of the more significant events in our history!

Below is a quick trip down memory lane of some of the memorable events from 2006-2008:

- in 2006, house prices peak
- in early 2007, house sales collapse
- April 2007, New Century Financial Corp., the largest subprime lender, files for bankruptcy
- Sept 2007, Fed cuts interest rates and the stock markets peak
- Jan 2008, Bank of America agrees to buy Countrywide (terrible decision in hindsight)
- March 2008, fire sale of Bear Stearns to JP Morgan
- Sept 2008, government nationalizes Fannie and Freddie
- Sept 2008, Lehman Brothers files for bankruptcy - the largest in US history
- Sept 2008, Fed bails out AIG (one days after Lehman bankruptcy)
- Sept 2008, big banks get bailed out with Troubled Asset Relief Program (TARP)
- Jun 2008 to March 2009, S&P500 falls 50%
- Nov 2008, Fed initiates quantitative easing - an effort to push down interest rates and boost economic activity.

Chapter 11: Investments – Equities – Current Holdings

The Big Three Equity Holdings:

- Eurobank
- Fairfax Total Return Swaps
- Poseidon/Atlas/Seaspan

For context, Fairfax has a total investment portfolio of about $56 billion, with fixed income investments of $40 billion and equity holdings of $16.3 billion.

Three equity holdings dominate all the others in size and together they total $5.5 billion or 34% of the total equity portfolio. In the first part of Chapter 11, we review each of these three holdings.

	Fairfax's Top 3 Equity Holdings		
	July 11, 2023		
		Value	Size
1.)	Poseidon/Atlas	$2,035	12%
2.)	Eurobank	$2,031	12%
3.)	FFH TRS	$1,434	9%
	Total Top 3	**$5,500**	**34%**
	Total All Equity	**$16,300**	
	Top 3 equity holdings = 34% of total		

Eurobank – EUROB.AT

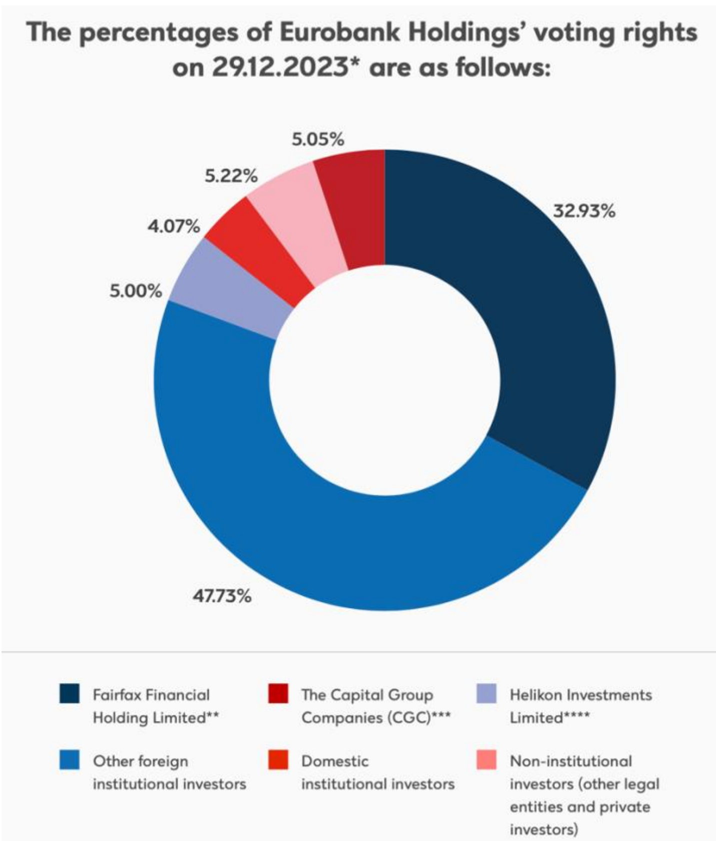
Feb 3, 2024

How many shares does Fairfax own?

It looks like I have been underestimating the number of shares of Eurobank that Fairfax owns/controls. I think the miss might be shares held as 'Asset Value Loan Notes' from the Riverstone Barbados sale.

Shares owned/controlled by Fairfax = 1.2237 billion = 3.716 billion x 32.93%

Eurobank Holdings Shareholding Structure



*As of 14/09/2023, due to a share capital increase following the exercise of stock option rights, the new total of the company's listed shares that are tradeable on the Athens Stock Exchange amounts to 3.716.479.777 common registered shares, for which the investment community was informed on **12.09.2023** by Eurobank Holdings, through a relevant corporate announcement.

**Based on the information received, from the company "Fairfax Financial Holding Limited", for which the investment community was informed on 20.07.2021 and on 26.07.2021 by Eurobank Holdings, through relevant corporate announcements.

July 11, 2023

Eurobank's stock is once again hitting all-time highs (€1.595 today). It is now tied with Poseidon/Atlas as Fairfax's largest equity holding. Time to do a review of what has been Fairfax's best performing equity holding over the past couple of years. This review will focus on the numbers and will be mostly forward looking.

For a historical look at Fairfax's investment in Eurobank go to 'Chapter 12: Geographies' and read the two posts on Greece.

Who is Eurobank?

Eurobank is one of the largest banks in Greece. Its core markets are Greece, Bulgaria and increasingly Cypress. It is recognized as being one of the best managed banks in Greece.

Management Presentation: 1H-2023

https://www.eurobankholdings.gr/-/media/holding/omilos/grafeio-tupou/etairikes-anakoinoseis/2023/2q-2023/2q2023-results-presentation.pdf

Of interest, Eurobank, Grivalia Hospitality and Eurolife are all joined at the hip.

Let's start by looking at the big picture.

What are prospects for the Greek economy?

Greece is positioned very well right now. The Greek economy turned the corner a couple of years ago now. Tourism is booming. As is the property market. Prime Minister Mitsotakis (center-right) was just re-elected with another majority for a second consecutive 4-year term. This ensures the significant economic (pro-market) reforms to the Greek economy will continue. Greece is expected to have one of the better performing economies in Europe over the next couple of years. This is a very positive backdrop for Eurobank.

How much of Eurobank does Fairfax own?

Fairfax owns 32.2% of Eurobank (1.166 billion shares). A stake worth $2 billion today.

Timeline of key events for Fairfax and Eurobank:

- Dec 2014: investment #1 in Eurobank of $444 million for 12.5% position.
- Nov 2015: investment #2 in Eurobank (recapitalization) of $389 million for 17% position.
- Dec 2015: purchase of 80% of Eurolife from Eurobank for $360 million.
- May 2019: Eurobank recapitalization / merger with Grivalia Properties - Fairfax owns 32.4%

Importantly, Eurobank is Fairfax's minority partner in both Eurolife and Grivalia Hospitality.

- July 2022: Fairfax increases stake in Grivalia Hospitality from 33.5% to 78.4% (purchased from Eurobank) for $195 million

How important is Eurobank to Fairfax?

Eurobank is similar in size to Poseidon/Atlas as Fairfax's largest equity holding. With a market value of about $2 billion, Eurobank represents 12% of Fairfax's total equity holdings of $16.3 billion.

What is the trend for earnings at Eurobank?

Earnings have been on a steady upwards trajectory in recent years. Management is guiding to earnings of €0.22/share in 2023. Management is conservative with their forecasts. Analysts are expecting earnings to come in around €0.24/share in 2023.

Eurobank Earnings

		change		
	per share	per share	%	
2023E	€ 0.24	€ 0.06	33%	Analyst estimates
2023E	€ 0.22	€ 0.04	22%	Management guide
2022	€ 0.18	€ 0.07	64%	
2021	€ 0.11			

How has the stock price of Eurobank performed?

Eurobank's stock price has been spiking higher - it is up 176% over the past 30 months. The market value of Fairfax's position in Eurobank is up $1.3 billion over the past 30 months, or $56 per Fairfax share. Clearly, Mr. Market is recognizing and rewarding the improving fundamentals and results at Eurobank.

Fairfax & Eurobank: 30 month performance

	Stock Price		Value of	Change in Value		30 Month Change in Value	
	Euro	US$	Position	$	%	$	%
July 11, 2023	€ 1.595	$1.742	$2,031	$688	51%	$1,294	176%
Dec 31, 2022	€ 1.055	$1.152	$1,344	$208	18%		
Dec 31, 2021	€ 0.891	$0.974	$1,135	$398	54%	$56 per FFH share	
Dec 31, 2020	€ 0.579	$0.632	$737				

Shares owned by Fairfax	1,166	million
Exchange rate (July 2023)	1.092	

How is Eurobank stock valued today?

The stock is trading at a forward price earnings of 6.65, a price to tangible book value of 0.83 and a return on tangible equity of 12.5%. Despite the 176% increase over the past 30 months, Eurobank's stock still looks cheap (sound familiar?).

Eurobank Valuation			
July 11, 2023			
	Price July 11 '23	Earnings Estimate	PE
Per Share	€ 1.595	€ 0.24	6.65
	Price July 11 '23	TBV Estimate	P/TBV
Per Share	€ 1.595	€ 1.92	0.83
	Earnings Estimate	TBV Estimate	ROTE
Per Share	€ 0.240	€ 1.92	12.5%

Note: I used the analysts guide for EPS for 2023 of €0.24/share.

Morgan Stanley currently has a price target for Eurobank of €2.10/share = $2.29/share. With shares trading at €1.595 today this suggests 32% upside. Currently 79% of analysts who follow Eurobank have the stock rated 'Overweight'. Of interest, if Eurobank traded at €2.10/share, Fairfax's position would be worth $2.675 billion.

How is Eurobank valued on Fairfax's books?

Eurobank is not a mark-to-market holding. Since Jan 1, 2020, it has been a consolidated holding (equity accounted). On March 31, 2023, Eurobank had a carrying value at Fairfax of $1.6 billion. As of today, there is an excess of $400 million of market value over carrying value ($17/share pre-tax). This excess is not captured in Fairfax's reported financial results (although they do highlight it in their commentary). This is a good example of where Fairfax's book value is understated.

Eurobank - Excess of Fair Value over Carrying Value			
July 11, 2023			
	Share Price	Value of Position	
Market Value	$1.742	$2,031	
Carrying Value	n/a	$1,632	From FFH Q1 2023 Earnings Report
Excess		**$399**	
		$17	Per Fairfax share

How do results at Eurobank flow though to Fairfax?

Dividends: Eurobank currently does not pay a dividend. Eurobank would like to start paying a dividend in 2024. In Q1-2023, Eurobank said they are targeting a minimum payout ratio of 25% - for both dividend and buybacks - in 2024.

Let's assume Eurobank goes with a payout ratio of 20% for the dividend. This would likely mean an annual dividend of around €0.048/share. In this scenario, Fairfax would start receiving dividends of $61 million per year.

For context, Fairfax currently receives about $135 million in dividends per year from all their various holdings. A dividend from Eurobank would increase this amount by 45%. This would be significant for Fairfax. Something to watch for in 2024.

Eurobank - Possible Dividend Payout				
			FFH	Total
	Annual Dividend Est		Shares	Payout
2024	€ 0.048	$0.052	1,166	$61

Share of profit of associates: Eurobank is a big reason we are seeing 'share of profit of associates' at Fairfax spike to over $1 billion per year in recent years. In the future, as Eurobank grows earnings, this should help push 'share of profit of associates' at Fairfax even higher.

Eurobank Share of Profit of Associates			
July 11, 2023			
	Fairfax Share		
	$	%	
2023E	$320	22%	My current estimate
2022	$263	62%	
2021	$162	n/a	
2020	-$12		

Investment Gains: As Eurobank gets fully valued, Fairfax could sell down its large position. That would crystallize any 'excess of fair value over carrying value'. Today the 'excess' is $400 million.

How much has Fairfax earned from its investment in Eurobank?

Fairfax is up about $935 million or 85% over the 8.5 years it has owned Eurobank (including the Grivalia transaction – see Prem's quote below).

Fairfax's Gain on Eurobank from Inception			
July 11, 2023			
	Share Price	Value of Position	
Market Value	$1.74	$2,031	July 11, 2023
Average Cost	$0.94	$1,096	From FFH 2021 Annual Report
Gain	**$0.80**	**$935**	
	85%		

Comments from Prem about Eurobank from the 2019AR.

> "The animal spirits are coming back to Greece and we think the Greek economy and Greek companies will thrive. Eurobank should benefit!! Our cost of 1.2 billion shares of Eurobank after the Grivalia transaction is now 94¢ versus a book value of approximately 135¢ per share post the transaction. At year end, Eurobank was selling at 68% of book value and 6.5x normalized earnings. We still believe it will be a good investment for us." *Prem Watsa – Fairfax 2019AR*

Conclusion

Despite getting off to a terrible start in 2014, Eurobank is turning into a very good investment for Fairfax. This has happened because of the hard work put in over many years by the Eurobank team in Greece, led by CEO Fokion Karavias and Vice Chairman George Chryssikos. Having a supportive, financially strong, long-term oriented and patient partner in Fairfax has also helped greatly. Most importantly, Eurobank is poised to perform well in the coming years. Given it is such a large holding this should benefit Fairfax shareholders greatly.

Making the initial investment in Eurobank also had important added benefits for Fairfax. It led Fairfax to buy 80% of Eurolife which has been an exceptional investment. It also led them to buy a 78.4% stake in Grivalia Hospitality (it is still early days on this investment). Importantly, Fairfax is viewed as being a trusted and strong foreign investor and partner in Greece.

Eurobank: Details of the Hellenic Bank Acquisition

August 31, 2023

Eurobank increased its ownership in Hellenic Bank to more than 50%. Its purchases in August (taking control over 30%) now need to be approved by regulators in Cypress. Once this happens (mid-year 2024?), Eurobank will be required to execute a mandatory tender offer for the 44.7% of Hellenic Bank it does not already own.

- Eurobank spent €152 million in 2021 and 2022 to purchase 29.2% of Hellenic Bank.
- In August, Eurobank is planning to spend an additional $253.3 million which, once approved by regulators, will increase their ownership to 55.3%.
- Upon approval from regulators, if the mandatory offer is €2.35/share, it will cost Eurobank up to €434 million to purchase the remaining 44.7% of Hellenic Bank.
- This would put the total cost for Eurobank to acquire 100% of Hellenic Bank at €839 million or €2.03/share.

Of interest, from continuing operations, Hellenic Bank earned €80 million in Q3 and €222 million YTD, 2023. Tangible book value per share is €3.21.

- https://www.hellenicbank.com/-/media/hbc/announcements/2023/november/9m-financial-results/financial-results-9m-2023-en.pdf

Eurobank - Hellenic Bank - History and Cost to Secure 55.3% Stake

		Ownership		Shares	Amount Paid		
	Date	%	Cumulative	Million	/ Share	Total €	Seller
1	June 21, 2021	9.9%		40.8	€ 0.80	€ 32.60	Third Point HRF
2	2H 2021	2.7%	12.6%	11.2	€ 0.80	€ 32.60	Third Point HRF
3	Nov 20, 2022	13.4%	26.0%	55.3	€ 1.26	€ 70.00	Wargaming Group
4	Dec 30, 2022	3.2%	29.2%	13.2	€ 1.27	€ 16.74	Senvest Management
5	Aug 23, 2023	17.3%	46.5%	71.4	€ 2.35	€ 167.90	Poppy Sarl (PIMCO)
6	Aug 25, 2023	1.6%	48.1%	6.6	€ 2.35	€ 15.50	Senvest Management
7	Aug 31, 2023	6.8%	54.9%	28.0	€ 2.35	€ 65.90	Wargaming Group
8	Aug 31, 2023	0.4%	55.3%	1.7	€ 2.37	€ 4.00	Wargaming (Mgmt)
	Total			**228.3**	**€ 1.78**	**€ 405.24**	
	Est cost for remaining shares		44.7%	184.5	€ 2.35	€ 433.61	Mandatory tender offer
	Est total cost for Hellenic		100%	412.8	€ 2.03	€ 838.85	

Below is a link to an article that provides an overview of Eurobank's investment in Hellenic Bank:

Eurobank locks in 50%+ of Hellenic Bank via Wargaming

https://www.cbn.com.cy/article/2023/8/30/729742/eurobank-locks-in-50-of-hellenic-bank-via-wargaming/

Fairfax Total Return Swaps – 1.96 million shares

January 31, 2024

The total return swap (TRS-FFH) position is becoming one of Fairfax's best investments ever. As we begin 2024, the position is up another $250 million. The investment has increased more than $1.3 billion since inception (late 2020/early 2021). Wow!

"We think this will be a great investment for Fairfax, perhaps our best yet!" This is what Prem said in his letter in the 2020 annual report when first describing this investment. Clearly, Fairfax was thinking big when they made this investment.

The genius of this single investment is still lost on many investors/analysts. Probably because the TRS is a non-traditional type of investment. So, it is largely ignored by investors/analysts in their analysis of the company and its potential impact on future earnings.

Fairfax - Total Return Swap	FFH Share	TRS Market	Annual Increase in Value (US$)	
1.96 mill shares	Price	Value	Total	/Share
Q4 '20/Q1 '21	$373	$731	n/a	n/a
Dec 31, 2021	$492	$965	$233	$10
Dec 31, 2022	$594	$1,164	$200	$9
Dec 31, 2023	$921	$1,805	$640	$28
Jan 31, 2024	$1,050	$2,059	$254	$11
Three + Year Gain in Value			**$1,328**	**$57**
Position put on Q4-2020 and Q1-2021; Avg cost = $373/sh.				

Well let's do a deep dive on this investment to better understand just what I am talking about.

<u>What is the TRS-FFH investment?</u>

In late 2020 and early 2021, Fairfax purchased total return swaps giving it exposure to 1.96 million Fairfax shares with an average notional amount (cost) of US$373/share.

At the time, Fairfax had about 26.2 million effective shares outstanding, so this investment represented 7.5% of the company's shares. Effective shares outstanding at the end of Q3, 2023 dropped to 23.1 million so this investment now represents 8.5% of the company's shares.

Fairfax's equity portfolio is about $16.5 billion in size. The TRS-FFH position currently has a market value of $1.8 billion = 11% of the total equity portfolio. This is Fairfax's third largest equity position, slightly smaller than Poseidon and Eurobank. It is a very large investment for Fairfax.

Why did Fairfax make this investment?

Fairfax's stock was trading at a crazy cheap valuation in late 2020. It was, by far, the best investment opportunity available to Fairfax at the time. To state the obvious, it was an investment they understood very well. So, it was a very low risk and very high return opportunity.

Comments from Prem about the total return swap purchase from the 2020AR.

> "Throughout much of last year (2020) following the pandemic-induced market plunge, I made public statements to the effect that our belief was that Fairfax shares were trading in the market at a ridiculously cheap price. In the summer I backed that up by personally purchasing close to $150 million of shares. Additionally, following our value investing philosophy, since the latter part of 2020 Fairfax has purchased total return swaps with respect to 1.4 million subordinate voting shares of Fairfax with a total market value at the time of those agreements of $484.9 million ($344.45 per share). We think this will be a great investment for Fairfax, perhaps our best yet!" *P.Watsa FFH 2020AR*

Prem's answer to question from Mark Dwelle (RBC) on the Q4 conference call in Feb 2021.

> Mark Dwelle: "My second question relates to executing the total return swap with respect to Fairfax shares. I guess, I was just curious why you pursue that structure, rather than just buying back the stock, if you felt like that was the good opportunity? I mean, is this a capital constraint that you couldn't really buy back that much?"
>
> Prem Watsa: "We have to be careful, right? So not so much -- yes, we have to be very careful in terms of how much we can buy back. When we looked at Fairfax as a stock price and looked at everything else that we could buy, which is not over return swap on Fairfax. Right now, we paid US$344 per shares, our book value is $478. I mean, if you want the math, just on our book value basis, we'd have about $200 million gain. And Fairfax stock price for book value is worth another 200 million. We just think it's a terrific investment and our total return swap structure was a very good way for us to do it. And so we did it."

Why buy the TRS-FFH versus simply buying back stock?

Fairfax did not have the cash at the time to buy back a significant amount of Fairfax stock directly.

Again, from the Q4 2021 conference call.

> Mark Dwelle: "I don't disagree with you that it was a good a good strike price, I guess it was really -- the form of the transaction rather than just actually buying the shares, using a derivative instead is just -- it's a little bit unusual. I haven't usually seen that with most of the companies that I've followed. So that was really my main question."
>
> Prem Watsa: "Yes, so, Mark, our point is just that we wanted to keep up -- we could -- where you have more than $1 billion in cash and the only company once -- or almost have down $375

million, we just wanted to be financially sound, and in all ways, as opposed to use that cash at this point in time."

This investment demonstrates Fairfax's management team at their best:

- Rational: best available opportunity
- Opportunistic: buy when the stock was crazy cheap
- Creative: didn't have the cash to do a buyback. Hello TRS.
- Conviction: wanted to buy a significant stake. Hello TRS (leverage).

Simply a brilliant investment - especially given the circumstances.

What is the outlook and for this investment?

The outlook for this investment is very good. Despite the run up over the past 3 years, Fairfax's stock price still looks cheap. This means the value of the TRS-FFH could be understated today. Having a low starting point matters greatly when calculating future returns for an investment.

Three possible catalysts:

- Record consistent cash flow: It looks promising for the next three years.
- Lower share count: Average decline of around 1.5% per year looks like a good estimate.
- Multiple expansion: Over time, Mr. Market will likely come to understand and appreciate the Fairfax story.

All three happening together could drive Fairfax's stock price higher - which of course means the value of the TRS-FFH investment would also be driven higher. This investment is poised to continue to generate solid returns for Fairfax in the coming years.

What are sell-side analysts saying?

This group doesn't know how to model Fairfax's equity holdings. The FFH-TRS position is a head scratcher for this group. So, they ignore it. I am serious.

Most sell-side analysts estimate Fairfax will earn $140 to $150/share next year. That translates to a $300 million gain in the FFH-TRS position.

Most sell-side analysts estimate investment gains of about $500 to $600 million for Fairfax in 2024. That is for their total investment portfolio of $56.5 billion. Bonds and stocks. And FFH-TRS. Analyst estimates look very low.

What is the lesson here for investors?

Sell-side analysts are like a limb on the body of Mr. Market.

What does Ben Graham teach us about Mr. Market? He (she) is there to serve you – not to inform or advise you. Mr. Market often gets things wrong. You job as an investor is to profit from Mr. Markets mistakes.

A note on share buybacks

Capital allocation is one of the most important decisions for a management team. Fairfax has said they believe their stock is very undervalued. They have also said that as the hard market in insurance slows, they will look to use excess capital to buy back their stock more aggressively.

Fairfax is likely motivated to drive the share price higher. Every $100 increase in the share price equals a $200 million before-tax investment gain. The TRS-FFH investment makes share buybacks an even more compelling capital allocation decision for Fairfax.

Is the TRS-FFH investment like a buyback? The TRS-FFH is the next best thing to doing a big buyback. Buybacks are powerful because they improve per-share financial metrics: EPS & BVPS.

- Buybacks lower the denominator (per share). If the buyback is large and sustained – and pushes up the share price over time - the TRS position could gain significantly in value.
- At the same time, the TRS- FFH investment increases the numerator (earnings and BV).

Investors get a double benefit.

Comments from Prem about the total return swap position from the 2022AR.

"During 2022 the company entered into $217.4 notional amount of long equity total return swaps for investment purposes. At December 31, 2022 the company held long equity total return swaps on individual equities for investment purposes with an original notional amount of $1,012.6 (December 31, 2021 – $866.2), which included an aggregate of 1,964,155 Fairfax subordinate voting shares with an original notional amount of $732.5 (Cdn$935.0) or approximately $372.96 (Cdn$476.03) per share at December 31, 2022 and 2021. During 2022 the long equity total return swaps on Fairfax subordinate voting shares produced net gains of $255.4 (2021 – $222.7). Long equity total return swaps provide a return which is directly correlated to changes in the fair values of the underlying individual equities." *Prem Watsa – Fairfax 2022AR*

Comments from Prem about the total return swap position from the 2021AR.

"For our stock price to match our book value's compound rate of 18.2%, our stock price in Canadian dollars should be $1,335. And our intrinsic value exceeds book value, a principal reason being that our insurance companies generate huge amounts of float at no cost. This is the reason we continue to hold total return swaps with respect to 1.96 million subordinate voting shares of Fairfax with a total market value of $968 million at year-end." *Prem Watsa – Fairfax 2021AR*

Comments from Prem about the total return swap position from the 2020AR.

"Throughout much of last year following the pandemic-induced market plunge, I made public statements to the effect that our belief was that Fairfax shares were trading in the market at a ridiculously cheap price. In the summer I backed that up by personally purchasing close to $150 million of shares. Additionally, following our value investing philosophy, since the latter part of 2020

Fairfax has purchased total return swaps with respect to 1.4 million subordinate voting shares of Fairfax with a total market value at the time of those agreements of $484.9 million ($344.45 per share). We think this will be a great investment for Fairfax, perhaps our best yet!"

Here is how our stock price has done compared to the TSX and S&P500 (all including dividends):

	Fairfax (US$)	**TSX**	**S&P500**
5 years	(4.3)%	9.3%	15.2%
10 years	0.4%	5.8%	13.9%
15 years	8.2%	6.0%	9.9%
20 years	6.1%	6.2%	7.5%
35 years since inception	16.4%	8.1%	11.1%

"Investment returns are very sensitive to end date values, so with a stock price of only $341 per share at the end of December 2020, our five and ten year and longer returns have been affected. We expect this to change as Fairfax begins to reflect intrinsic values again. Nothing that a $1,000 share price won't solve!" *Prem Watsa Fairfax 2020AR*

Total Return Swap: Some Additional Details

The other major benefit of a total return swap is that it enables the TRS receiver to make a leveraged investment, thus making maximum use of its investment capital. Unlike in a repurchase agreement where there is a transfer of asset ownership, there is no ownership transfer in a TRS contract.

This means that the total return receiver does not have to lay out substantial capital to purchase the asset. Instead, a TRS allows the receiver to benefit from the underlying asset without actually owning it, making it the most preferred form of financing for hedge funds and Special Purpose Vehicles.

There are several types of risk that parties in a TRS contract are subjected to. One of these is counterparty risk. When a hedge fund enters into multiple TRS contracts on similar underlying assets, any decline in the value of these assets will result in reduced returns as the fund continues to make regular payments to the TRS payer/owner.

If the decline in the value of assets continues over an extended period and the hedge fund is not adequately capitalized, the payer will be at risk of the fund's default. The risk may be heightened by the high secrecy of hedge funds and the treatment of such assets as off-balance sheet items.

Both parties in a TRS contract are affected by interest rate risk. The payments made by the total return receiver are equal to LIBOR +/- an agreed-upon spread. An increase in LIBOR during the agreement increases payments due to the payer, while a decrease in LIBOR decreases the payments to the payer. Interest rate risk is higher on the receiver's side, and they may hedge the risk through interest rate derivatives such as futures.

https://corporatefinanceinstitute.com/resources/derivatives/total-return-swap-trs/

Poseidon - Atlas - Seaspan

June 28, 2023

Poseidon is the entity formed by Fairfax, the Washington Family, David Sokol and Ocean Network Express (ONE) that took Atlas private in March of 2023. To keep things simple, for now I am going to refer to Atlas as Atlas (and not Poseidon).

Atlas is one of Fairfax's largest equity holdings with a fair value of $2.04 billion and carrying value of $1.64 billion at March 31, 2023. At fair value, it is about 12.7% of Fairfax's total equity portfolio of $15.7 billion. It is a significant holding.

Who is Atlas?

Atlas is a global asset management company. Their business is deploying capital to create long term value for owners. Today, Atlas owns two businesses:

- Seaspan (91% of EBITDA): the largest independent owner and operator of shipping containers in the world
- APR Energy (9% of EBITDA): the largest owner and operator of gas turbines in the world.

Management Presentation - Feb 2023 https://filecache.investorroom.com/mr5ircnw_seaspan/1280/download/Atlas Investor Presentation February 2023 - v02.pdf

A Brief History: Seaspan to Atlas to Poseidon

1.) Seaspan (2005)

- Seaspan was founded by the Washington Family in 1999. In 2005, Seaspan Corporation was taken public and listed on the NYSE. Today, Seaspan is the largest independent owner and operator of containerships in the world with 13% market share. As of March 31, 2023, Seaspan's operating fleet consists of more than 140 containerships with a total capacity of over 1.1M TEU. With 67 vessels under construction, the total capacity increases to over 1.95M TEU on a fully delivered basis.

2.) APR Energy

- From 2015-2017, Fairfax invested about $460 million to purchase 67.8% interest in APR. In November of 2019, Fairfax sold APR to Atlas for $254 million in Atlas shares (22.9 million x $11.10/share). Fairfax unloaded a problem child, so it was a great deal for Fairfax. Sokol got ownership of a second company - this time an energy company.
- Atlas is still in the process of turning APR around. New CEO. New strategy: exit Argentina and shift to long term contracts.

3.) Atlas Corp (Nov 2019)

- Concurrent with the APR purchase, Atlas was created. It is now 'an asset management company' and its focus is 'deploying capital to create long term value for owners'. It was interesting listening on the conference call when this change was announced and the management team trying and explain what they were doing to a bunch of containership analysts.
- The analyst community was never able to fully grasp the vision of what Sokol and team were trying to accomplish. It was the case initially with Seaspan when they tried to make the company a less cyclical business (more akin to a leasing company). The pivot to an asset management company (with the purchase of APR) was even more baffling for analysts.

4.) Poseidon (March 2023)

- Taking Atlas private now allows Sokol and the management team the ability to take Poseidon in whatever direction they want. Trying to appease a small group of minority shareholders (and analysts) is like herding cats. Sokol is a bright guy. He is ambitious. And he has a lot to prove. This probably makes good sense for everyone. Especially given the current weakness (putting it politely) in the containership market.
- The funding for the buyout of minority shareholders was mostly provided by ONE, Seaspan's largest customer. Fairfax did not provide any additional funds.

Who owns Atlas?

- Fairfax (45%)
- Washington Family (22% plus $175 million more?)
- Ocean Network Express ONE (30% ish – had $1.4 billion max spend)
- Management: Sokol, Chen etc (%? plus $30 million more?)

Poseidon has what looks to be a pretty rock-solid ownership group: Understand the industry. Deep pocketed investors. Patient. Supportive. Long term focus. Sokol and the management team must be SO HAPPY that the take private transaction is completed.

Washington Family founded Seaspan in 1999. Seaspan was listed on NYSE in 2005. They have been a large shareholder of Seaspan ever since.

https://www.washingtoncompanies.com/about-us/#our-history

Ocean Network Express (ONE) was established in 2017 with the merger of 3 Japanese container shippers ('K' Line, MOL and NYK). With a fleet size of 1,505,181 TEU, ONE is the 7th largest containershipper in the world. It is part of 'THE Alliance'. It is Seaspan's largest customer (at 24%).

https://www.one-line.com/en/standard-page/ocean-network-express

Why did Fairfax decide to invest in Seaspan/Atlas?

1. a bet on the jockey: David Sokol, and his impressive long term track record.
2. an opportunity to partner with the Washington Family.
3. a solid value investment: Seaspan was trading at a very cheap valuation.

Comments from Prem about the Seaspan purchase from the 2017AR.

> "Late in 2017, we had the good fortune to be a partner with David Sokol and Dennis Washington, two outstanding businessmen with great track records, by investing in Seaspan. Dennis is the largest shareholder of Seaspan while David became its Executive Chairman in July 2017. David has one of the most outstanding records I have come across, as he built Mid American Energy from revenue of $116 million in 1991 to revenue of $11 billion in 2010, while net income increased from $27 million to $1.2 billion over the same period, representing a compound growth rate of 22.4% per year." *Prem Watsa – Fairfax 2017AR*

How much has Fairfax invested in Atlas?

Common shares:

- Fairfax owns 130.8 million shares of Atlas = 45.4% of shares outstanding. On Feb 1, 2023, Atlas had 287.8 million shares outstanding. Below is a summary of how Fairfax accumulated its shares, beginning in July 2018.

Fairfax's path to owning 130.8 million shares of Atlas

date	date			cost		
granted	exercised		shares	per share	total $	Comment
Feb-18	Jul-18	Warrants	38.46	$6.50	$250	
Jul-18	Mar-22	Warrants	25.0	$8.05	$201	Incentive to exercise warrants early
Jan-19	Jan-19	Warrants	38.46	$6.50	$250	
Nov-19	Nov-19	APR	22.9	$11.10	$254	
Apr-21	Jan-23	Warrants	5.0	$13.00	$65	Part of APR final?
Jun-21	Jan-23	Warrants	1.0	$13.71	$14	Incentive to exch debt for pref shares
			130.8	**$7.90**	**$1,034**	

Other investments in Atlas:

- In June 2021, Fairfax converted $600 million in secured debt to $300 million in unsecured debt (5.5%) and $300 million in preferred shares (7%) and 1 million warrants ($13.71 strike, which have since been exercised.

date	coupon		yield
Feb-18	$250	Debenture	5.50%
Jan-19	$250	Debenture	5.50%
Feb-20	$100	Debt	5.50%
Jun-21	$300	Debt	5.50%
Jun-21	$300	Preferred shares	7%

How has the equity part of the investment performed?

Common shares:

- Based on the take private price of $15.50/share, Fairfax made a fair market gain of $9.225/share or $1.2 billion or +117% on its common stock investment in Atlas since 2018.

avg cost	$7.90	per share
dividends	$1.625	per share
net cost	$6.275	per share
buyout price	$15.50	per share
fair value	$2,027	$15.50 x 130.8
gain	$9.225	117%
gain - $	$1,207	

Fairfax also has $300 million in debt that is paying $16.5 million in interest (5.5%). And they have $300 million in preferred shares that pay $21 million in dividends (7%).

Future prospects for Atlas/Poseidon?

Recent developments:

- Seaspan is in the middle of a dramatic increase in capacity. They have 67 new container ships coming in 2023 and 2024 that will increase capacity from 1.1 to 1.95 million TEU. This will make them larger than ONE (1.5 million TEU).
- At the same time:
    - weak macroeconomic background
    - rising cost of capital - spiking interest rates
    - charter rates for container ship rates have fallen dramatically.
    - the 3 ocean alliances look like they are in the process of disintegrating.
- So, it would be an understatement to say that there is a lot going on right now in Seaspan's business. They have long term charters on all new ships coming on line. And they have the financing lined up for the new builds.
- As discussed earlier, APR is still in turnaround mode.

My guess is 2023 and 2024 will be quiet years as Atlas focusses on execution at Seaspan and APR. I wonder if the headwinds (softness in the shipping container market and higher cost of capital) mute the expected earnings growth at Atlas. Probably. Having a very strong private ownership group is a real benefit given the current environment.

Conclusion

Fairfax has done exceptionally well so far with its investment in Atlas. It will be interesting to see how the next two years play out. Does the new build strategy deliver the expected growth in earnings? Do they further diversify the platform and create a third earnings stream? What does Sokol and the management team accomplish over the next 5 years?

___________-

Davis Sokol joined Seaspan in 2017. His claim to fame was as Chairman and CEO of MidAmerican Energy, a company he sold to Berkshire Hathaway in 2000. He remained at Berkshire Hathaway until 2011, when he retired.

CNBC TRANSCRIPT: David Sokol Defends His Controversial Lubrizol Stock Purchases
https://www.cnbc.com/2011/04/01/cnbc-transcript-david-sokol-defends-his-controversial-lubrizol-stock-purchases.html

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Atlas Take Private Correspondence

Sept 26, 2022: Letter from Poseidon to Atlas's board presenting final $15.50 offer and also discussing current macroeconomic environment:

https://www.businesswire.com/news/home/20220926005186/en/POSEIDON-ACQUISITION-CORP.-UNILATERALLY-INCREASES-ITS-BID-PRICE-TO-ACQUIRE-ALL-COMMON-SHARES-OF-ATLAS-CORP.-NOT-CONTROLLED-BY-ITS-MAJORITY-SHAREHOLDERS-TO-15.50-PER-SHARE-IN-CASH

LF Partners Letters to Buyout Group

Aug, 2022: Initial letter sent to buyout group
https://www.globenewswire.com/en/news-release/2022/08/15/2498181/0/en/LF-Partners-Charles-Frischer-Sends-Letter-to-Atlas-Corporation-Special-Committee.html

September 21, 2022: Follow-up letter sent to buyout group
https://www.accesswire.com/716784/LF-Partners-Charles-Frischer-Sends-Letter-to-Special-Committee-Requesting-Buyout-Group-and-Special-Committee-Agree-to-1650-Final-Price

Publicly Traded Equity Holdings

• Blackberry	BB
• Dexterra	DXT.TO
• Fairfax India	FIH-U.TO
• Foran Mining	FOM.V
• Mytilineos	MYTIL.AT
• Stelco	STLC.TO
• Thomas Cook India	THOMASCOOK.BO

BlackBerry – BB

July 31, 2023

This post will tell readers much more about me than Fairfax or BlackBerry. But I suspect many Fairfax shareholders share the same sentiments as me when it comes to Fairfax's investment in Blackberry. So, with that out of the way, here goes… Of all the topics on Fairfax, this is one of the hardest for me to write about. For some reason when I think of Fairfax and BlackBerry, it always causes a sinking feeling in my gut. As a result, I have posted little about BlackBerry over the years.

Fairfax made their first investment in BlackBerry in 2011. I followed them in at the time and bought Research in Motion, or RIMM, as BlackBerry was known at the time. However, after listening to my third RIMM conference call, it was clear to me that the senior team was in over their heads. Brilliant founders. But they appeared to be struggling (putting it politely) with how to run a large company in an industry that was being disrupted by Apple, Google (Android) and Samsung. So, I sold my medium sized position at a modest loss. Fairfax kept buying.

As an aside, buying BlackBerry actually turned out to be one of my best investments ever. It taught me about the cell phone industry. In 1H-2013, Apple got taken out behind the woodshed, trading down to $15/share (split adjusted price) on worries about succession (Steve Jobs had recently passed away) and a belief that Android and Samsung were going to take over the smartphone world. I started buying Apple in early 2013 and backed up the truck in June of that year. Apple turned into one of my best investments ever… and I have Fairfax and BlackBerry to thank for that.

Back to our story. BB has been an epic failure as an investment for Fairfax for a number of reasons:

- Poor analysis of company at the time of purchase - classic definition of a value trap.
- Completely mis-judged senior management at the time of purchase.
- Canadiana: I suspect what led Fairfax into BlackBerry and kept them there was a desire (back then) to help build another 'Canadian champion' (to go along with Recipe, and Abitibi).
- Throwing good money after bad: they kept buying more year-after-year as the news kept getting worse.
- Impaired both Prem's and Fairfax's reputation.

The good news is BlackBerry is now a small position for Fairfax with a market value of $234 million (at $5.00/share, where it was trading recently). I am ignoring the debentures of $330 million (the right to buy 55 million more shares at $6.00/share, as they are out of the money).

I follow BlackBerry very little today. I have tried to listen to the quarterly conference calls a couple of times. But I haven't been able to listen to a whole call - too much 'big hat no cattle' type of talk.

Blackberry recently announced that they were exploring 'strategic alternatives.' Initially this excited me. I thought great, this might be Fairfax's opportunity to exit the holding at a reasonable price.

And then I saw a letter from a disgruntled Blackberry shareholder who expressed concern that Prem would use his position on the board of BlackBerry to take it private at a cheap price. And I got that sinking feeling in my gut again.

Letter from concerned Blackberry shareholder
https://www.newswire.ca/news-releases/concerned-shareholder-urges-blackberry-board-to-guard-against-unfair-buyout-bids-and-oppose-watsa-as-director-as-board-considers-strategic-alternatives-887083805.html

Would Fairfax pony up the billions needed to take BlackBerry private? They have been investing billions the past couple of years increasing their stakes in existing holdings. They probably could come up with the money - perhaps they tap OMERS and/or CPIB as minority partners.

If Fairfax took BlackBerry private it could work out fabulously well. BlackBerry does have some interesting assets. I told you already I don't follow the company. So, I don't know.

What I do know is if Fairfax took BlackBerry private (and ponied up a bunch of new money) they would risk wiping out a bunch of the goodwill with investors that they have slowly been re-building the past couple of years. My view is some investments in a portfolio need to get sold. For psychological reasons. Get rid of the dogs and move on. I understand that is not a rational thing to say. BlackBerry does that to me.

So, we wait to see what the result of the 'strategic review' is. And pray that the senior team at Fairfax and Hamblin Watsa are thinking rationally.

Comments from Prem about Blackberry from the 2022AR.

"John Chen continues to strengthen BlackBerry in its two high growth markets – cybersecurity and embedded operating systems for the automotive industry. Within its Internet of Things, expanding further into verticals like medical, industrial and aerospace remain opportunities to accelerate growth. Its patent portfolio monetization is expected to occur in 2023 after some hurdles in 2022."
Prem Watsa – Fairfax 2022AR

Dexterra – DXT.TO

May 10, 2023

If I was Fairfax, what would be my next take-private equity purchase? Probably Dexterra. Yes, not a needle mover. But it would be a solid addition to their current collection of private companies.

Why? Dexterra looks very cheap (the stock), generates solid free cash flow and has solid growth prospects. And Fairfax has the cash.

<u>What is the Dexterra story?</u>

in 2018, Fairfax purchased Carillion Canada out of bankruptcy. The problem with Carillion was its UK parent went bankrupt. Fairfax paid about five times free cash flow for the Canadian operations. In 2020, Dexterra acquired Horizon North Logistics in a reverse takeover. Fairfax owned 49% of the combined company. This deal closed in May of 2020 (as Covid was raging). At the time, Dexterra's CEO, John MacCuish, set the audacious target for C$1 billion in revenue and C$100 million in EBITDA in the 'next few years.'

How is the company doing? After hitting a speed bump in 2022, Dexterra is on track to achieve both of their financial targets, perhaps as soon as 2024. As part of an updated 5-year vision just unveiled today at the AGM, a new C$2 billion revenue target has been set. The growth at Dexterra is being funded by internally generated cash and debt (which is reasonable). EBITDA conversion to free cash flow is expected to be 50%.

What was the speed bump in 2022? Inflation put two business segments on their ass:

1. IMF: Was not able to reprice contracts quick enough.
2. Modular Solutions: BC contracts did not have an inflation clause (CEO of this division has since left).

In Q1, 2023 we learned IMF profitability is getting back to targeted levels. In modular, the remainder of the unprofitable BC contracts will be run off in Q2 and Q3 (the financial hit was already largely booked in Q4, 2022). The turnaround in modular will likely be a late 2023 or 2024 story.

Bottom line, 2023 is shaping up to be a decent year for the company. More acquisitions are likely coming. Growth should pick up again in 2024. Dividend is a solid 6.8%. Chug, chug, chug.

<u>Management Presentations</u>:

AGM: https://dexterra.com/wp-content/uploads/2023/05/2023-AGM-Presentaion.pdf

Q2-2023: https://dexterra.com/wp-content/uploads/2023/08/Analyst-Presentation-Q2-2023.pdf

What are Dexterra's businesses?

It is a diverse collection of 3 businesses.

- Integrated Facilities Management (IFM): the growth engine
- Workforce Accommodations, Forestry, Energy Services (WAFES)
- Modular Solutions

This is Dexterra: https://dexterra.com/wp-content/uploads/2021/03/Dexterra_ServicingTheFuture_Brochure.pdf

Fairfax's Ownership of Dexterra

	2020	2021	2022	
Shares	31.8	31.8	31.8	million
Ownership	49%	49%	49%	
Carrying value	$115	$117	$103	million
	$3.62	$3.69	$3.24	per share
Market value	$161	$215	$127	million
	$5.06	$6.76	$4.01	per share

Comments from Prem about Dexterra from the 2022AR.

"Dexterra is on track to achieve its vision of becoming a leader in delivering quality solutions to create, manage and operate infrastructure. John MacCuish is retiring after an outstanding performance for us, from rescuing Carillion from bankruptcy to the merger with Horizon North to form Dexterra. A big thank you to John for his leadership and dedication to Dexterra and best wishes to him and his family for a long and healthy retirement. The new CEO Mark Becker has been a senior leader in the organization for several years and is supported by three strong business unit Presidents. Dexterra closed two important integrated facilities management acquisitions early in the year and, coupled with organic growth, this strategic business unit almost doubled in size in 2022. The workforce accommodations segment also continued to build market share and deliver strong profitability while capitalizing on higher activity levels in Canada's resource industries, although Dexterra's modular business experienced short-term profitability challenges given high inflation and supply chain disruptions. Management expects to continue to build its modular platform and diversify its product mix, with strong demand for social and affordable housing across Canada." *Prem Watsa – Fairfax 2022AR*

Comments from Prem about Dexterra from the 2020AR.

"In the third bucket, let's illustrate with Recipe, Fairfax India and Dexterra. These positions are fully consolidated into our financial statements – our balance sheet and income statement.

"The development of Dexterra's business was dramatically reshaped by the reverse takeover in May 2020 of Horizon North. Dexterra, now a listed public company and led by John MacCuish, has a vision to build a Canadian support services champion. Its activities include a comprehensive range of facilities management, workforce accommodations, and forestry and modular build capabilities, including being a leader in social housing projects. Dexterra has publicly stated that it is on course in the next few years for Cdn$1 billion in revenue and Cdn$100 million in EBITDA."
Prem Watsa – Fairfax 2020AR

Fairfax on the Acquisition of Horizon North Logistics from the 2020AR

"On May 29, 2020 Horizon North Logistics Inc. ("Horizon North") legally acquired 100% of Dexterra by issuing common shares to the company representing a 49.0% equity interest in Horizon North. The company obtained de facto voting control of Horizon North as its largest equity and voting shareholder and accounted for the transaction as a reverse acquisition of Horizon North by Dexterra. The assets, liabilities and results of operations of Horizon North were consolidated in the Non-insurance companies reporting segment. Horizon North, which was subsequently renamed Dexterra Group Inc. ("Dexterra Group"), is a Canadian publicly listed corporation that provides a range of industrial services and modular construction solutions." *Fairfax 2020AR*

Comments from Prem about Dexterra from the 2020AR.

"I am happy to report that we also made two significant private company investments in 2018/2019 – Dexterra and AGT. Dexterra, led by John MacCuish as CEO, is the new name for Carillion Canada which went into bankruptcy because of the bankruptcy of its parent in the U.K. Dexterra provides industry-leading facilities management and operation solutions across Canada, including maintenance solutions for over 50 million sq. ft. of high-quality infrastructure. This includes some of the country's largest airports, premier retail and commercial properties, corporate campuses, research and education facilities, large industrial sites, defence and public assets and state-of-the-art healthcare infrastructure. The company is also one of the country's largest reforestation contractors – planting over 40 million trees annually, it annually completes 4,400 hectares of forest thinning/brushing and 1,200 hectares of site preparation–it employs hundreds of firefighters, with an emphasis on Indigenous communities, and for the last 30 years it has been supplying and operating full-service remote workforce services. We were able to buy Dexterra at about 5x free cash flow." *Prem Watsa – Fairfax 2018AR*

Fairfax on the price paid to acquire Dexterra from the 2018AR

"Purchases of subsidiaries, net of cash acquired of $163.1 in 2018 primarily related to the acquisitions of Dexterra (100%) and Toys "R" Us Canada (100%)." *Fairfax 2018AR*

Fairfax India – FIH-U.TO

January 4, 2023

Fairfax India was launched in 2015. It has grown into a wonderful business for Fairfax.

- Solid collection of assets.
- Very well managed.
- Very good track record.
- Well positioned for the future.

In this post we are going to get into the weeds of how Fairfax India is valued by its parent, Fairfax.

How much of Fairfax India does Fairfax own?

When Fairfax India was launched in 2015, Fairfax owned 28.1%. My math says Fairfax now owns 43.0% of Fairfax India, which is an increase of more than 50% over the past 8 years. Fairfax India is also now a much larger company - common shareholders equity has increased from $1 billion at inception in 2015, to $2.8 billion at Sept 30, 2023, which is an increase of 180%. So today, Fairfax owns 50% more of a company that has increased in size by 180%.

That sounds great. But what does the math look like?

How many shares of Fairfax India does Fairfax actually own?

It can be a little confusing to understand exactly how many shares of Fairfax India that Fairfax actually owns. This is because some shares are held in an 'asset value note' that was put on when Fairfax sold RiverStone Barbados a couple of years ago.

On Feb 16, 2022, when they added to their position, Fairfax confirmed they 'beneficially owned, and/or exercised control or direction over' a total of 58.4 million shares of Fairfax India. I am assuming that is the number of shares they 'own' today.

Fairfax's Ownership Stake in Fairfax India		
September 30, 2023	**million**	
Fairfax India - Total shares outstanding	135.7	
Fairfax - Total shares owned	58.4	43.0%

A short history of the growth of Fairfax's ownership of Fairfax India (total shares and %) can be found at the bottom of this post.

Market value and carrying value

What is the market value that Fairfax uses to value its stake in Fairfax India?

To determine market value, Fairfax uses Fairfax India's stock price, which at Dec 31, 2023, was $15.20/share. This gives a total market value to Fairfax's position of $888 million.

What is the carrying value that Fairfax uses to value its stake in Fairfax India?

Carrying value is important. This is the value that finds its way into book value. And, as we know, book value is the 'holy grail' use by investors to value P/C insurance companies.

In the 2022AR, Fairfax said the carrying value for their investment in Fairfax India was $10.78/share, or $630 million (using my share count of 58.4 million).

What is the excess of market value over carrying value?

It appears Fairfax's book value is understating the market value of its stake in Fairfax India by about $250 million. (Yes, i know my dates are messed up… directionally, it appears Fairfax India's carrying value at Fairfax is low).

How Fairfax Values its ownership position in Fairfax India				
		Shares	**Total**	
	/ share	**mn**	**$mn**	
Market Value - Dec 31, 2023	$15.20	58.4	$888	Fairfax India's stock price
Carrying Value - Dec 31, 2022	$10.78	58.4	$630	From Fairfax's 2022AR
Excess of Market Value over Carrying Value			**$258**	

OK. Are we done? No. There is a wrinkle.

Fairfax India's stock price is a terrible measure to use to value Fairfax's stake in Fairfax India. And that is because Fairfax India's stock price trades at a severe discount to the fair value of the collection of companies that it owns.

My guess is accounting standards require Fairfax to report carrying value and market/fair value the way they do.

What should we do? Fairfax India has very good disclosures. We should simply use Fairfax India's book value - that is the best measure of what the collection of assets they own are actually worth.

What is the value of Fairfax's stake if we use Fairfax India's book value?

Fairfax India has a book value of $20.89/share (at Sept 30, 2023), which puts the value of Fairfax's stake at $1.22 billion (using my share count of 58.4 million). It appears Fairfax's book value is understating the value of its stake in Fairfax India by about $590 million. That is much larger than our previous estimate of $250 million.

An alternative way to value Fairfax's ownership position in Fairfax India				
Closer to actual 'fair value'?		Shares	Total	
	/ share	mn	$mn	
Book Value* - Sept 30, 2023	$20.89	58.4	$1,220	From Fairfax India's Q3 Report
Carrying Value - Dec 31, 2022	$10.78	58.4	$630	From Fairfax's 2022AR
Excess of Book Value* over Carrying Value			**$590**	
* Book Value as calculated by Fairfax India				

If we use a fair value of $1.22 billion, this suggests Fairfax India is Fairfax's 4th largest holding, along with Eurobank, Poseidon and FFH-TRS. These 4 holdings represent about 40% of Fairfax's total equity exposure.

<u>What does Prem think about Fairfax India's reported book value?</u>

Prem thinks that Fairfax India's intrinsic value is 'much higher' than its reported book value. If Prem is right, then the value of Fairfax's stake in Fairfax India is worth even more than $1.22 billion.

Below are Prem's comment from Fairfax's 2022AR:

> While the book value per share of Fairfax India is **$19.11** per share, we believe the underlying intrinsic value is much higher. Given the low market price for its shares, Fairfax India has taken the opportunity in the last four years to buy back 15.1 million shares for **$194** million at an average price of **$12.84** per share, including the three million shares it bought in 2022 for **$36** million or an average price of **$12** per share.

<u>Growth prospects</u>

Fairfax India reported a book value of $20.89/share at Sept 30, 2023. My guess is it will be well over $21 at Dec 30, 2023. Let's assume Fairfax India grows BV/share at 10% in 2024, which would be $2.10/share.

This would put Fairfax's share of growth in BV at $123 million ($2.10/share x 58.4 million shares). This would also deliver a (very rough) high teens ROE.

Estimating Fairfax Share of Fairfax India's Growth in BV in 2024					
			Shares	Growth	Rough
FIH.U Est BV/share at December 31, 2023		$21.00	mn	$ mn	ROE
Growth in BV/share in 2024	10%	$2.10	58.4	$123	19%
Est Fairfax Carrying Value - Dec 31, 2022		$630			

Is 10% growth in BV/share an aggressive assumption? No, I actually think it will prove to be conservative. Why?

- BIAL is now 47% of total investments at Fairfax India. Its value has gone sideways for the past 3 years - as a result of Covid. However, the airport is beginning its next significant growth phase (as second runway and recently completed Terminal 2 ramp up). An Anchorage IPO in 2024 could unlock significant value that has been building at BIAL.
- Two other private holdings in Fairfax India also might see IPO's in 2024: NSE and SIS, which would likely unlock more value for Fairfax India.
- The remaining holdings of Fairfax India are well run companies and should continue to increase in value.

If my rough math is accurate, Fairfax's stake in Fairfax India is poised to grow in value by about $123 million in 2024. Some of this value will show up in the 'share of profit of associates' bucket. However, like the past 8 years, a large part of the value will likely not show up in Fairfax's reported results. As a result, the gap between fair value and carrying value will continue to widen.

<u>Conclusion</u>

Since being launched in 2015, Fairfax India has quietly been growing like a weed. It is a great example of exceptional long term value creation by the team at Fairfax/Fairfax India/Fairbridge. However, the value creation has largely not been reflected/captured in Fairfax's accounting results - especially book value.

Fairfax India is a great example of how book value at Fairfax is understated. There are likely more examples.

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<u>Warren Buffett on book value</u>

Warren Buffett published the book value for Berkshire for the last time in the 2018AR. I wonder how much longer book value will serve as a useful tool for investors to value Fairfax's share price.

> "The fact is that the annual change in Berkshire's book value – which makes its farewell appearance on page 2 – is a metric that has lost the relevance it once had. Three circumstances have made that so. First, Berkshire has gradually morphed from a company whose assets are concentrated in marketable stocks into one whose major value resides in operating businesses. Charlie and I expect that reshaping to continue in an irregular manner. Second, while our *equity holdings* are valued at market prices, accounting rules require our collection of *operating companies* to be included in book value at an amount far below their current value, a mismark that has grown in recent years. Third, it is likely that – over time – Berkshire will be a significant repurchaser of its shares, transactions that will take place at prices above book value but below our estimate of intrinsic value. The math of such purchases is simple: Each transaction makes per-share intrinsic value go up, while per-share book value goes down. That combination causes the book-value scorecard to become increasingly out of touch with economic reality." *Warren Buffett – Berkshire Hathaway 2018AR*

<u>A short history of Fairfax's investment in Fairfax India</u>

Fairfax India was launched in 2015. At inception, Fairfax invested a total of $300 million ($10/share) for a 28.1% ownership position. Fairfax India did a second capital raise in January 2017 (at $11.75/share) and Fairfax participated to keep its ownership position of similar size (it was 30.2% at the end of 2017. Fairfax has also received two performance fees in shares of Fairfax India (2018 and 2021). Today Fairfax owns 58.4 million shares of Fairfax India. My rough math says they paid a total of $539 million or an average of $9.23/share.

Share count at Fairfax India peaked at 152.9 million at December 31, 2018. Since that time, the share count has come down 11.2% to 135.7 million. With the stock trading well below book value, Fairfax India has been taking out shares on the cheap. Smart.

With Fairfax's share count going up and Fairfax India's share count coming down, Fairfax has increased its ownership interest in Fairfax India from 28.1% in late 2015 to 43.0 at Sept 30, 2023. That is an increase of more than 50% over the past 8 years. That is a meaningful increase.

History of Fairfax's Investments in Fairfax India

	Fairfax India	Fairfax's Transaction History			Fairfax's Ownership of Fairfax India		
	Total	Number	Cost		Cumulative		
Date	Shares	of Shares	$/sh	$mn	Shares	%	Comments
Dec 31, 2015	106.7	30.0	$10.00	$300	30.0	28.1%	IPO @ $10/share
Dec 31, 2016	104.9			$0	30.0	28.6%	
Jan 13, 2017		12.3	$11.75	$145	42.3		Private placement at $11.75/sh
Dec 31, 2017	106.7	1.50	$11.75	$18	43.8	30.2%	Fairfax 12.34mn + OMERS = 29.7mn
Mar 9, 2018	104.9	7.7	$0.00	$0	51.5		FFH performance fee = 7.66mn shares
Dec 31, 2018	152.9			$0	51.5	33.7%	
Dec 31, 2019	152.6	0.1	$12.00	$1	51.6	33.8%	
Dec 31, 2020	149.5			$0	51.6	34.5%	
Mar 5, 2021		0.5	$0.00	$0	52.1		FFH performance fee = 546,263 shares
Aug 11, 2021	-7.0			$0			SIB = 7.046mn shares at $14.90/share
Dec 31, 2021	141.2			$0			
Feb 26, 2022		5.4	$12.00	$65	57.5	42.1%	FFH purchase at $12 (OMERS?)
Dec 31, 2022	138.3	0.9	$12.00	$11	58.4	42.2%	
Sep 30, 2023	135.7			$0	58.4	43.0%	
Total	**million**	**58.4**	**$9.23**	**$539**			

Timeless article on Fairfax India that was written in Feb 2020. It could have been written last week. Covid hit Fairfax India especially hard as an airport (BIAL) is their largest asset – by far.

Woodlock House Family Capital: Epictetus, India and Patience

https://www.woodlockhousefamilycapital.com/post/epictetus-india-and-patience

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Fairfax India: Summary of 'total existing Indian investments'

At Sept 30, 2023, Fairfax India held total investments with a fair value of $3.376 billion. If we adjust for Q4 transactions (increase in BIAL and decrease in IIFL Finance):

- BIAL (manages BLR Airport) = 47%
- All other holdings = 53%

Fairfax India: Summary of Fair Value of Holdings and Size Weightings						
US$ million	**Sept 30**		**Q4**	**Adjusted**		**Fair Value**
Investment	**Fair Value**		**Transactions**	**Fair Value**		**of Fairfax**
BIAL	$1,408	42%	$175	$1,583	47%	**Share**
IIFL Finance	$570	17%	-$154	$416	12%	**43.0%**
Sanmar	$301	9%		$301	9%	
CSB Bank	$321	10%		$321	10%	
NSE	$176	5%		$176	5%	
Other Investments	$600	18%		$600	18%	
Total Fair Value	**$3,376**			**$3,376**		**$1,452**

In Q4, Fairfax purchased 7% of BIAL and sold down its position in IIFL Finance by 27%

Fairfax India

- Shareholders equity = $2.833 billion
- Debt = $500 million

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Summary of key metrics for Fairfax India (from 2022AR)

Here is a snapshot of Fairfax India's performance since it began:

$ millions except per share amounts:	2022	2021	2020	2019	2018	2017	2016	2015	CAGR[1]
Book value per share	$ 19.11	$ 19.65	$ 16.37	$ 16.89	$ 13.86	$ 14.46	$ 10.25	$ 9.50	8.5%
Income	237.5	693.5	(13.0)	712.7	166.5	609.7	128.6	65.3	
Net earnings (loss)	191.4	494.5	(41.5)	516.3	96.4	452.5	107.8	40.9	
Return on equity	7.1%	18.9%	(1.7)%	22.0%	4.5%	28.2%	10.3%	4.0%	11.7%[2]
$ billions:									
Total assets	3.4	3.6	3.1	3.2	2.7	2.7	1.3	1.0	16.2%
Investments	3.2	3.5	3.0	3.2	2.7	2.6	1.1	1.0	16.2%
Common shareholders' equity	2.6	2.8	2.4	2.6	2.1	2.1	1.1	1.0	12.9%
Shares outstanding (millions)	138.3	141.2	149.5	152.6	152.9	147.4	104.9	106.7	

(1) Since Fairfax India's inception on January 30, 2015, when it raised $1.03 billion at $10 per share. From an initial value of $9.62 (after IPO expenses), book value per share has compounded at 9.0% annually.

(2) Simple average of the return on equity for each of the eight years.

Summary of Fairfax India's exceptional long term track record (at Sept 30, 2023)

- 'Total existing Indian Investments' CAGR = 13.0%
- 'Total monetized Indian Investments' CAGR = 17.5%

From Fairfax India's Q3 Interim Report - Page 32
- https://www.fairfaxindia.ca/wp-content/uploads/FIH-2023-Q3-Interim-Report-Final.pdf

Track Record

The table below provides a summary of the company's existing and monetized Indian Investments, including their compounded annualized return in U.S. dollars since the company's inception:

		September 30, 2023					
Existing Indian Investments:	**Initial investment date**	**Ownership %**	**Cash consideration** [1]	**Fair value**	**Net change**	**Cumulative interest and dividends** [2]	**Compounded annualized return** [3]
Public Indian Investments:							
Common stocks:							
IIFL Finance [4]	December 2015	20.9 %	105,337	570,160	464,823	22,024	26.7 % *
IIFL Securities [4]	December 2015	27.7 %	51,055	88,116	37,061	13,935	10.4 % *
5paisa [4]	December 2015	24.9 %	16,603	40,641	24,038	—	18.4 % *
Fairchem Organics [5]	February 2016	52.8 %	29,741	97,330	67,589	2,108	23.2 %
CSB Bank	October 2018	49.7 %	169,492	321,233	151,741	—	15.0 %
Other	May 2022	< 1.0 %	3,386	2,163	(1,223)	15	(27.3)%
			375,614	1,119,643	744,029	38,082	20.9 %
Private Indian Investments:							
Common stocks:							
NCML	August 2015	91.0 %	188,288	50,359	(137,929)	823	(16.2)%
Sanmar	April 2016	42.9 %	199,039	301,293	102,254	—	11.5 %
NSE	July 2016	1.0 %	26,783	176,789	150,006	15,048	33.5 %
Saurashtra	February 2017	51.0 %	30,018	54,081	24,063	4,565	10.7 %
BIAL	March 2017	57.0 %	727,982	1,408,403	680,421	2,241	12.0 %
IH Fund [6]	January 2019	—	13,986	14,137	151	4,423	6.4 %
Seven Islands	March 2019	48.5 %	83,846	143,413	59,567	—	12.8 %
Maxop	November 2021	67.0 %	51,448	55,530	4,082	—	5.2 %
Jaynix	February 2022	70.0 %	32,504	45,974	13,470	—	23.7 %
Other Indian Fixed Income	November 2021	—	7,395	7,345	(50)	475	3.1 %
			1,361,289	2,257,324	896,035	27,575	9.8 %
Total existing Indian Investments			1,736,903	3,376,967	1,640,064	65,657	13.0 %

Monetized Indian Investments:	**Initial investment date**	**Last sale date**	**Cash consideration** [1]	**Cash proceeds** [1]	**Cash proceeds less cash consideration**	**Cumulative interest and dividends** [2]	**Compounded annualized return** [3]
Partially monetized [7]**:**							
IIFL Finance [4]	December 2015	June 2023	6,613	30,512	23,899	1,383	25.2 % *
Fairchem Organics [5]	February 2016	February 2022	7,787	45,585	37,798	86	49.7 %
			14,400	76,097	61,697	1,469	36.5 %
Fully monetized:							
360 ONE (formerly IIFL Wealth) [4]	December 2015	May 2023	107,044	243,465	136,421	40,492	16.7 % *
Other	March 2018	January 2023	178,762	282,564	103,802	9,298	28.0 %
Privi Speciality [5]	August 2016	April 2021	54,975	164,895	109,920	1,985	27.1 %
Sanmar Bonds [8]	April 2016	December 2019	299,000	433,873	134,873	—	11.0 %
			639,781	1,124,797	485,016	51,775	16.6 %
Total monetized Indian Investments			654,181	1,200,894	546,713	53,244	17.5 %
**** Aggregate: IIFL Finance, IIFL Securities, 5paisa and 360 ONE (formerly IIFL Wealth)***							*20.8 %*

Anchorage Infrastructure Investments Holdings

December 31, 2023

Anchorage is a subsidiary of Fairfax India (100% owned).

Fairfax India created Anchorage in 2019. Fairfax India intends to use Anchorage to grow its investments in airports and infrastructure in India. To seed the new investment, Fairfax India transferred 43.6% of its ownership in BIAL.

In 2021, Anchorage brought on its first partner. An 11.5% interest in Anchorage was sold to OMERS for $129.2 million. This transaction suggests the total value of Anchorage is $1.123 billion.

Anchorage is awaiting regulatory approval to do an IPO in India. When completed (hopefully in 2024), this transaction will provide an important update of the total value of Anchorage (and BIAL).

Comments from Fairfax India's 2022AR:

> "In June 2019, Fairfax India created a 100% owned subsidiary in India named Anchorage Infrastructure Investments Holdings (Anchorage). It is intended that this company will be Fairfax India's flagship investment vehicle for airports and other infrastructure investments in India and that all the shares it owns in Bangalore International Airport (BIAL) will eventually be transferred to Anchorage.
>
> "In September 2021, Fairfax India, as previously agreed, transferred 43.6% out of the 54% that it owns in BIAL to Anchorage and OMERS (the pension plan for municipal employees in the Province of Ontario, Canada) invested $129.2 million to acquire from Fairfax India an 11.5% interest on a fully diluted basis in Anchorage. This resulted in OMERS indirectly owning approximately 5% of BIAL. At that time, this transaction valued 100% of BIAL at $2.6 billion.
>
> "Fairfax India intends to complete an IPO of Anchorage, although we did not move forward on this in 2022 as we are awaiting regulatory approvals.
>
> "Once Anchorage is listed, the proportion of the publicly listed investments in Fairfax India will increase from the current 39.2% to 79.8% of the overall portfolio." *Fairfax India 2022AR*

Comments from Fairfax India's Q3 Interim Report:

> **Non-controlling interests**
>
> "Net earnings attributable to non-controlling interests of $31 and $10,291 during the third quarter and first nine months of 2023 (2022 - $87 and $63) principally related to net unrealized gains on Anchorage's investment in BIAL.

"The company shall use commercially reasonable efforts to list Anchorage by way of an IPO in India, subject to regulatory approvals and market conditions on or before September 2025. If the valuation of Anchorage upon closing of the IPO is below approximately $1.1 billion (at period end exchange rates) (91.6 billion Indian rupees), then OMERS' ownership in Anchorage will increase to a maximum of 15.0% and the company's ownership in Anchorage will decrease to a minimum of 85.0% (effective ownership interest in BIAL will decrease from 57.0% at September 30, 2023 to a minimum of 50.5%). If Anchorage does not list by way of an IPO in India by September 2025, then OMERS' ownership in Anchorage will remain at 11.5%." *Fairfax India Q3 Interim Report*

Valuation and Interim Consolidated Financial Statement Impact

"On May 9, 2023 Fairfax India announced it entered into an agreement to acquire additional equity interest in BIAL through FIH Mauritius and on June 21, 2023 the company completed the acquisition of a 3.0% equity interest in BIAL for cash consideration of $75,000 (approximately 6.2 billion Indian rupees). Under the same agreement, the company has also agreed to acquire an additional 7.0% equity interest in BIAL for additional cash consideration of $175,000, subject to certain performance conditions by BIAL and other closing conditions, which are expected to be assessed in the fourth quarter of 2023.

"At September 30, 2023 the company held a 57.0% equity interest in BIAL (December 31, 2022 - 54.0%), and its internal valuation model indicated that the fair value of the company's investment in BIAL was $1,408,403 (December 31, 2022 - $1,233,747). At September 30, 2023 the company continued to hold 43.6% out of its 57.0% (December 31, 2022 - 43.6% out of its 54.0%) equity interest in BIAL through Anchorage. As a result, the company's fully-diluted equity interest in BIAL was 52.0% (December 31, 2022 - 49.0%)." *Fairfax India Q3 Interim Report*

Additional information on the aviation sector in India

GMR Airports Infrastructure Limited, publicly traded, might be a good comparable for Anchorage.

G M Rao (Chairman, GMR Group): "GMR Group operated airports, during FY 2022-23, handled a total of more than 100mn passengers (Including passengers handled at Delhi, Hyderabad, Mopa, Cebu and Medan airports). Our Indian portfolio of airport assets handled ~87mn passengers during FY 2022-23, thus forming a 26.6% market share of all India traffic."

Website: https://investor.gmrinfra.com

Bangalore International Airport Limited (BIAL)

December 31, 2023

What is Fairfax's 4th largest equity holding? At December 31, 2023, with a value of about $630 million, it looks to me like it is BIAL. BIAL is owned entirely within Fairfax India so it tends to get ignored as a core holding at the Fairfax (parent) level. But the fact it is ignored does not mean it does not exist.

For good reason, Prem calls BIAL the 'crown jewel' of Fairfax's various equity holdings in India. BIAL is a very high quality asset - it is a trophy asset (very hard to secure a control position). It is well managed. And it looks exceptionally well positioned to benefit from the expected growth of the economy in India in the coming decades. So, in this post, let's shine a light on this important holding to see what we can learn.

Who is BIAL?

The best place to go to get information on BIAL is Fairfax India's web site (start with the Q3 Interim Report and the 2022 Annual Report):

- https://www.fairfaxindia.ca

Here is how Fairfax India described BIAL in their Q3, 2023 Interim Report:

> "Bangalore International Airport Limited ("BIAL") is a private company located in Bengaluru, India. BIAL, under a concession agreement with the Government of India until the year 2068, has the exclusive rights to carry out the development, design, financing, construction, commissioning, maintenance, operation and management of the Kempegowda International Airport Bengaluru ("KIAB") through a public-private partnership. KIAB is the first greenfield airport in India built through a public-private partnership." *Fairfax India - Q3 Interim Report*

KIAB (also known as BLR Airport) is the third largest airport in India and the largest airport in south India. Bangalore, the centre of India's high-tech industry, is known as the 'Silicon Valley of India'. KIAB was recently voted best domestic airport in India (go to the bottom of this post for a link to the article).

> The History And Rise Of Bangalore International Airport
>
> - https://simpleflying.com/bengaluru-airport-history/

A review of the fair value of the assets owned by Fairfax India

Fairfax India owns assets with a fair value at Sept 30, 2023 of $3.38 billion. In Q4, Fairfax India increased its ownership in BIAL by 7% (at a cost of $175 million) and sold down its position in IIFL Finance by 27%. Including these two recent transactions, BIAL represents about 47% of all assets in Fairfax India. BIAL is a massive holding for Fairfax India.

Fairfax owns 42.8% of Fairfax India. This puts the fair value of Fairfax's stake in Fairfax India at about $1.45 billion.

Fairfax India: Summary of Fair Value of Holdings							
US$ million	Sept 30		Q4	Adjusted			Fair Value
Investment	Fair Value		Transactions	Fair Value			of Fairfax
BIAL	$1,408	42%	$175	$1,583	47%		Share
IIFL Finance	$570	17%	-$154	$416	12%		42.8%
Sanmar	$301	9%		$301	9%		
CSB Bank	$321	10%		$321	10%		
NSE	$176	5%		$176	5%		
Other Investments	$600	18%		$600	18%		
Total Fair Value	**$3,376**			**$3,376**			**$1,445**
In Q4, Fairfax purchased 7% of BIAL and sold 27% of IIFL Finance							

<u>What is the math that gets BIAL to a $631 million valuation for Fairfax?</u>

As we mentioned earlier, Fairfax does not own BIAL directly - its position is held entirely through Fairfax India.

<u>Estimating the total value of BIAL</u>:

- At September 30, 2023, Fairfax India held an equity interest in BIAL of 57% with an estimated fair value of $1.408 billion. This values 100% of BIAL at $2.6 billion. In Q4, Fairfax India purchased another 7% BIAL from Siemens for $175 million; this transaction values 100% of BIAL at $2.5 billion. Given this is the most recent transaction, this is the number we will use to value Fairfax's stake.

<u>Estimating the fair value of Fairfax's stake in BIAL</u>:

- As of December 31, 2023, Fairfax India owned 59% of BIAL (on a fully-diluted equity basis). Fairfax owns about 42.8% of Fairfax India. Therefore, Fairfax owns about 25.25% of BIAL (59% x 42.8%), with a value of $631 million ($2.5 billion x 25.25%). This makes BIAL the 4th largest equity holding of Fairfax (after Eurobank, Poseidon and FFH-TRS).

Calculating Fairfax's Ownership Interest in BIAL			
December 31, 2023	Ownership %	Value $mn	
Estimated value of 100% of BIAL		$2,500	Using recent transaction value
Fairfax India's Fully-Diluted Equity Interest in BIAL	59.0%	$1,475	Does not include OMERS 5% interest
Fairfax's Equity Interest in Fairfax India	42.8%		Total from all sources
Fairfax's Equity Interest in BIAL		$631	= 25.25% of the total

From Fairfax India’s Q3 interim report:

> “At September 30, 2023 the company held a 57.0% equity interest in BIAL (December 31, 2022 - 54.0%) and its internal valuation model indicated that the fair value of the company's investment in BIAL was $1,408,403 (December 31, 2022 - $1,233,747).”
>
> “At September 30, 2023 the company held 43.6% out of its 57.0% (December 31, 2022 - 43.6% out of its 54.0%) equity interest in BIAL through Anchorage. As a result, the company's fully-diluted equity interest in BIAL was 52.0% (December 31, 2022 - 49.0%). Refer to note 8 (Total Equity, under the heading Non-controlling interests) for further discussion on Anchorage.”

<u>How much did it cost Fairfax India to secure a 59% interest in BIAL?</u>

Fairfax India made their first purchase in BIAL in 2016. Since then, they have made 5 more purchases. Over the past 8 years, Fairfax India has spent a total of $902 million for 64% of BIAL.

In 2019, Fairfax India also sold a 5% interest to OMERS for $134 million. The sale was made via Anchorage (a subsidiary of Fairfax India).

Fairfax India’s fully-diluted equity position in BIAL (of 59%) cost a total of $768 million.

		BIAL: Transaction Timeline					**Implied**
		December 31, 2023				**Deal**	**Value of**
		Purchase Summary		**Deal**	**Cumulative**	**Price**	**Airport**
Date		**Buyer**	**Seller**	**Size**	**Ownership**	**US$mn**	**US$mn**
2016	Mar	Fairfax India	GVK Power	33%	33%	$336	$1,018
2016		Fairfax India	Zuerich Airport	5%	38%	$49	$980
2017	Jun	Fairfax India	GVK Power	10%	48%	$200	$2,000
2018	Mar	Fairfax India	Siemens	6%	54%	$67	$1,117
2023		Fairfax India	Siemens	3%	57%	$75	$2,500
2023	Dec	Fairfax India	Siemens	7%	64%	$175	$2,500
	Fairfax India - Equity Interest				**64%**	**$902**	
		Sale Summary					
2019	Dec	OMERS	Fairfax India	5%	59%	$134	$2,680
	Fairfax India - Fully-Diluted Equity Interest				**59%**	**$768**	

<u>What has been the return on the 8-year investment in BIAL?</u>

The fair value of Fairfax India’s 59% stake in BIAL is about $1.475 billion. Its cost is $768 million. The simple return is about $707 million.

As reported by Fairfax India, the CAGR on this investment since inception has been 12.8% (to Sept 30, 2023).

Est of Return on 8-Year Investment in BIAL	Fairfax India Interest			Fairfax Interest
December 31, 2023				
Fair Value Estimate	%	$mn		42.8%
Value of BIAL (Dec 2023)	100%	$2,500		
Value of BIAL (Dec 2023)	59%	$1,475		$631
Cost Summary				
Fairfax India - Equity Interest	64%	$902		
Less: OMERS / Anchorage Interest	5%	$134		
Fairfax India - Fully-Diluted Equity Interest	59%	$768		$329
Total Return for Fairfax India (2016 to 2023)		$707		$303

What is the carrying value of Fairfax India at Fairfax?

This is where things get even more interesting.

At December 30, 2022, Fairfax had a carrying value for all of Fairfax India of $630 million (58.4 million shares x $10.78/share) - that is what is reflected in Fairfax's book value. (Of interest, my math says the total cost to Fairfax since late 2015 of its various investments in Fairfax India has been about $539 million. So, carrying value for Fairfax India is slightly higher than Fairfax's cost basis? For an asset that has increased significantly in value of the past 8 years? That is something we will review in a future post.)

Carrying value significantly understates the value of Fairfax's stake in Fairfax India today.

BIAL represents about 47% of Fairfax India. This gives us a ball-park estimate for the carrying value of BIAL at Fairfax today of about $300 million ($630 million x 47%).

Summary: Fairfax's 25.25% interest in BIAL has a fair value of about $630 million and a carrying value of about $300 million. That is a significant difference. And as the value of BIAL grows in the coming years, that difference will likely grow even larger.

The very low carrying value of Fairfax India (including BIAL), is one good example of how the book value of Fairfax today is significantly understated.

Management

In 2017, Fairfax India paid up to get a controlling position in BIAL. They quickly overhauled management and installed Hari Marar as Managing Director and CEO. BIAL is exceptionally well managed. BIAL is a great example of the strong management team at Fairfax India.

Since taking over in 2017, the management team at BIAL has done an exceptional job. See 'recent news' articles below for some current examples.

From Fairfax India's 2017AR:

"In July 2017 Fairfax India acquired the final 10% of BIAL owned by GVK for $200 million, the higher price being justified by this purchase enabling Fairfax India and the other remaining shareholders to reconstitute BIAL's Board, to appoint the best qualified person as BIAL's CEO, and generally to allow it to be managed according to Fairfax India's standards of corporate governance and guiding principles.

"Subsequently, three new directors with expertise in airport and airline management and finance were appointed to the Board of BIAL, and Hari Marar, the former COO of BIAL, was appointed as its new Managing Director and CEO."

Conclusion

BIAL has been a solid investment for Fairfax India. Over the past 8 years, it has grown into the 4th largest equity holding of Fairfax. It has a carrying value that is less than half of its fair value.

BIAL is a very high quality asset. It is also exceptionally well managed. It is also perfectly positioned to benefit from India's growth in the coming years and decades. The runway for this investment is very long.

Most importantly, Fairfax (via Fairfax India) has a control position in this very rare asset. That is almost priceless - and likely the reason Prem calls BIAL a 'crown jewel' asset for Fairfax.

Recent news on BLR Airport:

Dec 2023: Bengaluru airport - master plan with renovation of T1, new place for T3 by 2030
- https://indianexpress.com/article/cities/bangalore/bengaluru-airport-master-plan-renovation-9049746/#

Dec 2023: BLR Airport Secures 'Best Domestic Airport' Title
- https://www.bengaluruairport.com/corporate/media/news-press-releases/blr-airport-secures-best-domestic-airport-title-at-travel-leisure-india-s-best-awards-----

Dec2023: BLR Airport's Terminal 2 earns UNESCO's recognition as one of the 'World's Most Beautiful Airports'
- https://www.bengaluruairport.com/corporate/media/news-press-releases/terminal---earns-unesco-s-recognition-as-one-of-the-world-s-most-beautiful-airports-and-

Dec 2023: Bengaluru airport most profitable in India in FY23
- https://www.moneycontrol.com/news/technology/bengaluru-airport-most-profitable-in-the-country-in-fy23-ahmedabad-incurs-highest-losses-11859721.html#

Ownership structure of BIAL at December 31, 2023

BIAL Ownership Structure				
December 31, 2023				
Fairfax India Equity Interest			64%	
	Direct	20.4%		
	Anchorage	43.6%		11.5% of Anchorage is owned by OMERS
Siemens			10%	
KSIIDC			13%	Karnataka Government
AAI			13%	Airport Authority of India
Total			**100%**	
Fairfax India's Full-Diluted Equity Interest = 59%				

Fairfax open to acquiring AAI's 13% stake in Bangalore Airport: Hari Marar

- https://www.thehindubusinessline.com/economy/logistics/fairfax-open-to-acquiring-aais-13-stake-in-bangalore-airport-marar/article67466405.ece

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Prem's Letter, Fairfax 2022AR:

"**While the book value per share of Fairfax India is $19.11 per share, we believe the underlying intrinsic value is much higher**. Given the low market price for its shares, Fairfax India has taken the opportunity in the last four years to buy back 15.1 million shares for $194 million at an average price of $12.84 per share, including the three million shares it bought in 2022 for $36 million or an average price of $12 per share."

Fairfax India Q3, 2023 Interim Report: Details of BIAL and Anchorage Subsidiary

"Non-controlling Interests: In 2019 the company formed Anchorage as a wholly-owned subsidiary of FIH Mauritius, intended to provide investment related services to support the company in investing in companies, businesses and opportunities in the airport and infrastructure sectors in India. On September 16, 2021 the company transferred a 43.6% equity interest in BIAL from FIH Mauritius to Anchorage and subsequently sold 11.5% (on a fully-diluted basis) of its interest in Anchorage to OMERS for gross proceeds of $129,221 (9.5 billion Indian rupees). Upon closing of the transaction, the company's ownership in BIAL was comprised of 10.4% held through FIH Mauritius and 43.6% held through Anchorage, representing effective ownership interest of 49.0% on a fully-diluted basis.

"At September 30, 2023 the company continued to hold 43.6% out of its 57.0% (December 31, 2022 - 43.6% out of its 54.0%) equity interest in BIAL through Anchorage. As a result, the company's fully-diluted equity interest in BIAL was 52.0% (December 31, 2022 - 49.0%)."

A history of financial transactions at BIAL

Date		Buyer	Seller	Stake/ Size	Transaction Price Rs (crore)	US$	Implied Value of Airport US$	New Total Ownership Stake Buyer %	Seller %	Comments
		BIAL: Transaction Timeline								
		December 2023								
1999	May	KSIIDC (Karnata government)		13%	Memorandum signed: public-private parnership					
		AAI (Airport Authority of India)		13%	KSIIDC and AAI have same ownership position in Dec 2023.					
		Private Companies (TBA)		74%	See next entry for split of private companies in 2001.					
2001	Nov	Siemens		40%	Siemens lead team wins bid to build airport					
		L&T IDPL		17%	Ownership split of 74% private ownership					
		Zuerich Airport		17%						
2005	July	Construction begins								
2008	May	First flight								
2009	Nov	GVK Power	Zuerich Airport	12%	484	$96	$800	12%	5%	Flughafen Zuerich AG
2009	Dec	GVK Power	L&T Infrastruc	17%	686			29%	0%	L&T Infrastructure Development Projects
2011	Aug	GVK	Siemens	14%	614	$135	$964	43%	26%	8.6% premium to 2009 price paid
2013	Dec	Re-named Kempegowda International Airport (KIA) after Kempe Gouda, founder of Bangalor								Threat from Changi & Tatas forces premium
2013	Dec	Phase 1 expansion completed (expansion terminal called Terminal A1); increased passenger capacity to 25 million								
2016	Mar	Fairfax India	GVK Power	33%	2,202	$336	$1,018	33%	10%	GVK sold to pay down debt; closed Mar 2017
2016		Fairfax India	Zuerich Airport	5%	320	$49	$980	38%	0%	Closed Mar 2017
2017	Jun	Fairfax India	GVK Power	10%	1290	$200	$2,000	48%	0%	
With purchase Fairfax now has controlling stake in BIAL and overhauls management; explains what looks like overpay given recent transactions										
2018	Mar	Fairfax India	Siemens	6%		$67	$1,117	54%	20%	
2019	Dec	OMERS	Fairfax	5%		$134	$2,680			Position controlled by Fairfax via Anchorage
2023		Fairfax India	Siemens	3%		$75	$2,500	57%	17%	
2023	Dec	Fairfax India	Siemens	7%		$175	$2,500	64%	10%	Additional 5% controlled via Anchorage

Timeline for BLR Airport

Foran Mining – FOM.TO

December 12, 2023

Foran completes private placement. Fairfax purchased 2.439 million shares at C$4.10.
At December 29, 2023, Fairfax owned 21% of Foran (on a fully diluted basis).

March 4, 2023

In August 2021, Fairfax invested C$100 million in Foran Mining - an exploration and development company. At the time, the purchase was a bit of a head scratcher. An exploration company? Mining? Canada? Really?

Eighteen months later, what have we learned?

1. The energy transition to EV's is happening. And lots of inputs, especially copper, are likely going to be in short supply looking out 2 or 3 years. This could spike copper prices.

2. 'The story' at Foran continues to get better. They are discovering more, large deposits (copper, zinc, gold and silver). Mine development is progressing, with initial production scheduled to begin in 2025. More savvy, deep pocketed partners are signing on. The company is looking to 'graduate' its stock listing from the venture exchange to the TSX.

What is Fairfax's exposure? Fairfax owns 23% of Foran.
- Aug 2021: purchased 55.6 million shares at C$1.80 at a total cost of C$100 million.
- Oct 2022: exercised 16 million warrants at C$2.09 at a total cost of C$33 million.

Shares of Foran Mining closed Friday at C$3.88, near a 52-week high.
- 71.6 million shares x C$3.88 = C$277 million = US$204 million.
- the value of Fairfax's initial investment has doubled over the past 18 months.

What does it mean for investors in Fairfax? The story at Foran Mining continues to get better. Yes, it is still early days. And there will be lots of volatility. The significant exposure to copper could turn this investment into a big winner in the coming years for Fairfax shareholders. Foran Mining is looking like yet another example of the team at Fairfax hitting the ball out of the park with their equity purchase decisions over the past couple of years.

Foran Mining Corporate Presentation

Forecast for accelerated EV sales and copper demand – Aug 2022

Mytilineos – MYTIL.AT

July 26, 2023

Mytilineos shares have been on a tear in 2023. Here is a short update of what it means for Fairfax.

Who is Mytilineos?

- Ticker: MYTIL.AT (trades on the Athens stock exchange)
- Stock price: $36.68 (July 26, 2023)
- Market cap: €5.07 billion
- Dividend = €1.24 = 3.4%

From the company's web site: "MYTILINEOS Energy & Metals is a global industrial and energy company covering two business Sectors: Energy and Metallurgy. The Company is strategically positioned at the forefront of the energy transition as an integrated utility, while already established as a reference point for competitive green metallurgy at the European and global level. It has a consolidated turnover and EBITDA of €6.35 billion and €823 million, respectively, and employs more than 5,442 direct and indirect employees in Greece and abroad."

Corporate Presentation - Jun 2023

https://www.mytilineos.com/media/k5lj10q0/corporate_presentation_june_2023.pdf

How much of Mytilineos does Fairfax own?

Fairfax owns 9.19 million shares (including the exchangeable bonds) with a value of $372 million. This makes the company a top 15 holding in Fairfax's equity portfolio.

Fairfax's Ownership of Mytilineos

	Shares	Share Price		Value	
Date	millions	€	$	mill $	
26-Jul-23	9.19	€ 36.68	$40.53	$372	includes exch bonds

Fairfax made its first investment in Mytilineos in 2012 and 2013 (around a €30 million stake at the time). In November of 2022, Fairfax owned 3.99 million shares. In December 2022, Fairfax more than doubled their stake:

- They purchased 2.7 million shares at €18.50.
- They purchased exchangeable bonds that give them the right to buy another 2.5 million shares at €20.

Fairfax is now the second largest shareholder of Mytilineos.

How has the investment performed since Fairfax added to their position in December 2022?

Fairfax's position is up $171 million or 85% over the past 8 months (to July 26, 2023). I am including the exchangeable bonds in this calculation as they are well in the money.

Mytilineos - estimate of gains on position since Dec '22					
			Total	1.105	€ to US$
	Share Price		Value	Increase	
	€	$	mill $	mill $	%
22-Dec-22	€ 19.84	$21.92	$201		
31-Dec-22	€ 20.30	$22.43	$206	$5	2%
26-Jul-23	€ 36.68	$40.53	$372	$166	81%
Increase since Dec 22, 2022				**$171**	**85%**
Total Shares		9.19		Incl exch bonds	

What is Fairfax's average cost on its total position? (very rough)

My guess is Fairfax's average cost on its total Mytilineos position is less than €13.10/share. This estimate does not include dividends, which Mytilineos has paid since 2018.

- It was reported by Mytilineos in October 2013 that Fairfax had purchased 4.97 million shares at €5.13/share for a total of €25.5 million. My assumption below is the 3.99 million shares Fairfax held in Nov 2022 are part of this original purchase.

Mytilineos - estimated cost of total position				
Since inception (2013 + 2022)			1.105	€ to US$
	Total	Cost		
	Shares	per share	total €	mill $
start - estimate	3.99	€ 5.13	€ 20.47	
22-Dec-22	2.70	€ 18.50	€ 49.95	
Exch bonds	2.50	€ 20.00	€ 50.00	
Total	**9.19**	**€ 13.10**	**€ 120.42**	**$133**

Articles on Fairfax's initial and most recent investments in Mytilineos.

October 21, 2013: Canada's Fairfax buys Mytilineos stake in second bet on Greece
https://www.reuters.com/article/us-greece-fairfax/canadas-fairfax-buys-mytilineos-stake-in-second-bet-on-greece-idUSBRE99K05H20131021

December 13, 2022: Fairfax becomes the 2nd largest shareholder in MYTILINEOS
https://www.mytilineos.com/news/company-news/fairfax-becomes-the-2nd-largest-shareholder-in-mytilineos

Stelco – STLC.TO

November 9, 2023

Update: On Nov 8, 2023, Stelco announced another special dividend of C$3/share, along with the regular quarterly dividend of $0.42/share. Fairfax will earn US$32 million, payable Nov 28, 2023.

In November of 2018, Fairfax invested US$193 million in Stelco, buying 13 million shares at C$20.50. At the time, it was a deeply contrarian purchase. I did not like it. It screamed 'old Fairfax' to me: buy a bad business in a bad industry. Boy, was I wrong.

What has made this such a good investment for Fairfax?

The CEO of Stelco, Alan Kestenbaum. Since buying Stelco out of bankruptcy in 2017 (via Bedrock Industries) he has been putting on a clinic in capital allocation. (I'll come back to this.)

Stelco Corporate Presentation Q3-2023

https://s201.q4cdn.com/143749161/files/doc_earnings/2023/q3/presentation/Q3-2023-Earnings-Presentation-FINAL.pdf

Here is a little more information of Kestenbaum's initial investment in Stelco in 2017.

Purchase of Stelco out of bankruptcy: Bedrock gets steelmaker for less than $500 million

https://www.thespec.com/business/stelco-deal-bedrock-gets-steelmaker-for-less-than-500-million/article_da943b70-1a93-5a35-acb4-92a6da05946a.html?

How has the investment performed for Fairfax?

Over the past 5 years, Fairfax has received dividend payments (regular and special) from Stelco of $106 million. This has reduced Fairfax's cost base from $193 million to $87 million.

Fairfax's investment in Stelco has a market value today (Nov 9) of $398 million. Fairfax's investment in Stelco is up $311 million or 358%. That is an amazing return over a 5 year period.

Estimating Fairfax's Total Return on Stelco Investment	**Share Price C$**	**Total Value C$ mn**	**Total Value US$ mn**	
Initial investment in Stelco	$20.50	$267	$193	Nov 2018
Regular dividends received since 2018			$38	
Special dividends received since 2018			$68	
Adjusted cost of Stelco investment (after dividends)			**$87**	
Current value of investment	$42.24	$549	$398	Nov 9, 2023
Increase in value from adjusted cost			**$311**	**358%**

What are prospects for Stelco?

Very good; just like for the big US steelmakers.

Kestenbaum - Schooling the Steel Industry on Capital Allocation

What did Stelco do with the earnings windfall from 2021 and 2022? He bought back stock 38% of shares outstanding. And he did not overpay. That was freaking brilliant.

Fairfax's ownership in Stelco has increased from 14.7% to 23.6% - with no new money invested.

Stelco Share Count	total shares (millions)	YOY change		2 year change %	FFH % ownership
Date		shares	%		
31-Dec-20	88.7				14.7%
31-Dec-21	77.3	-11.4	-13%		16.8%
31-Dec-22	55.1	-22.2	-29%	-38%	23.6%
Fairfax owns	13				

Two other brilliant moves by Kestenbaum:

- April 2020 - Minntac deal: 8-year supply agreement with option to purchase 25% of Minntac (the largest iron ore mine in the US) for $100 million – done when Covid was raging.
- June 2022: real estate sale of 'Stelco lands' for C$518 million. The timing of this sale is looking brilliant - at what might be close to the peak of Canada's real estate bubble.

Comments from Prem about Stelco from the 2022AR.

> "2022 was an active and successful year for Alan Kestenbaum and the talented team at Stelco. The company ended the year with its second-best fiscal result since going public despite an approximately 50% decline in steel prices over the summer. Stelco is benefiting from the Cdn$900 million it has invested in its Lake Erie Works mill since 2017, which has made the mill one of the lowest-cost operators in North America. Stelco entered 2022 with an extremely strong balance sheet and put its capital to good use, completing three substantial issuer bids during the year, thereby repurchasing approximately 29% of its outstanding shares. These repurchases have resulted in Fairfax's ownership increasing to 24% from 17% at the beginning of the year. In addition to share repurchases, Stelco paid a Cdn$3 per share special dividend and increased its regular dividend to Cdn$1.68 per share from Cdn$1.20 per share. Stelco maintains over Cdn$700 million of net cash on its balance sheet and we anticipate that it will continue to be active both investing in its operations and efficiently returning excess capital to shareholders. We are excited to continue as a significant investor in Alan Kestenbaum's leadership at Stelco." *Prem Watsa – Fairfax 2022AR*

Details of Stelco's Hamilton land sale in 2022, for proceeds of $518 million.

"Stelco Holdings Inc. (TSX: STLC) ("Stelco" or the "Company") announced today that its wholly-owned subsidiary, Stelco Inc., has successfully closed a sale-leaseback transaction with an affiliate of Slate Asset Management ("Slate"). Stelco Inc. has sold the entirety of its interest in the approximately 800-acre parcel of land it occupies on the shores of Hamilton Harbour in Hamilton, Ontario to Slate for gross consideration of $518 million. In conjunction with the sale, Stelco Inc. has entered into a long-term lease arrangement for certain portions of the lands to continue its cokemaking and value-added steel finishing operations at its Hamilton Works site in Hamilton, Ontario."

https://www.thespec.com/news/hamilton-region/all-of-stelco-s-hamilton-land-sold-in-deal-that-would-see-it-transformed-into/article_17a333af-8198-5f97-9866-8c61ed8f799f.html?

Details of Stelco's agreement with US Steel in 2020 to securing long term supply for iron ore pellets.

Stelco Announces Option To Acquire 25% Interest In Minntac, The Largest Iron Ore Mine In The United States, And Entry Into Long-Term Extension Of Pellet Supply Agreement With U.S. Steel

"Stelco will pay US$100 million, in cash, to U.S. Steel in consideration for the Option (the "Initial Consideration"). The Initial Consideration is payable in five US$20 million installments, with the first installment paid upon closing of the Option Agreement and the remaining four installments payable every two months thereafter. Upon the exercise of the Option, Stelco would pay a net exercise price of US$500 million."

Transaction Highlights

- Secures long-term future of Stelco's steel production and solidifies Stelco's low-cost advantage
- Provides supply of high-quality iron ore pellets from a well-understood and consistent source for the next eight years, or longer if the Option is exercised
- Increases annual pellet supply to level required for Stelco's higher production capacity following this year's blast furnace upgrade project
- Supports Stelco's tactical flexibility model to deliver highest margin outcomes based on prevailing market conditions
- Creates a secure pathway for Stelco to become a vertically integrated player in the future through ownership in a low-cost iron ore source which is the largest producing iron ore mine in the Mesabi iron range
- Structured in stages that will preserve Stelco's strong balance sheet and financial flexibility

https://investors.stelco.com/news/news-details/2020/Stelco-Announces-Option-to-Acquire-25-Interest-in-Minntac-the-Largest-Iron-Ore-Mine-in-the-United-States-and-Entry-into-Long-Term-Extension-of-Pellet-Supply-Agreement-with-U.S.-Steel-04-20-2020/default.aspx

Thomas Cook (India) Limited – THOMASCOOK.BO

December 5, 2023

Thomas Cook (India) Limited (TCIL) has had a pretty spectacular year so far in 2023. YTD, shares of TCI have increased in value by 116%. It appears people in India are travelling again.

Thomas Cook India				
	Dec 4	Dec 31	Change	
	2023	2022	INR	%
Share Price	₹ 154.00	₹ 71.15	₹ 82.85	116%

Who is TCIL?

TCIL is the leading omnichannel travel company in India offering a broad spectrum of services including Foreign Exchange, Corporate Travel, MICE, Leisure Travel, Value Added Services and Visa Services.

Company presentation: business results to Sept 30, 2023 (scroll down after clicking link)

https://resources.thomascook.in/downloads/SEINTIMATIONSinvestorpresenation.pdf?_gl=1*1tufk2e*_ga*NjU3NjA5NzI4LjE3MDE3NTMyMzY.*_ga_FKZBDJSK02*MTcwMTc1MzIzNi4xLjEuMTcwMTc1MzM0Mi41OS4wLjA.

How much of TCIL does Fairfax own?

On December 1, 2023, Fairfax sold 40 million shares of TCIL for proceeds of $67 million. After this sale, Fairfax continues to own 300.3 million shares, or 63.8%, of TCIL. (This assumes TCIL did not buy back any of the shares Fairfax sold.)

Fairfax's Ownership Position in Thomas Cook India (Dec 4, 2023)		shares mn
TCI	Total Shares Outstanding	470.4
Fairfax	Total Shares Owned	300.3
	Ownership share	63.8%

Fairfax's ownership position in TCIL had a market value of $554 million on Dec 4, 2023. TCIL is the 7th largest equity holding for Fairfax.

Fairfax : Market Value of Thomas Cook India Position	INR	US$
Share Price - Dec 4, 2023	₹ 154.00	$1.85
Shares Owned by Fairfax (mn)		300.3
Market Value (US$mn)		$554
Currency rate (INR to US$):	0.01199	

Accounting: Market Value (MV) and Carrying Value (CV)

Given Fairfax owns more than 50% of TCIL, from an accounting perspective, TCIL is valued in Fairfax's financial statements at carrying value and not market value.

At Dec 1, 2023, the excess of market value over carrying value was $339 million (pre-tax). Fairfax is sitting on a significant unrealized gain on TCIL that is not captured in its current book value.

Fairfax: Excess of Market Value over Carrying Value For Thomas Cook India Position

Shares	Market Value Dec 1, 2023			Carrying Value Sept 30, 2023		Excess MV to CV
mn	INR	US$	Total $	US$	Total $	US$
300.3	₹ 146.70	$1.76	$528	$0.629	$189	$339
Currency rate (INR to US$):		0.01199				

How much did Fairfax make on its recent sale of TCIL shares?

On December 1, 2023, Fairfax sold 40 million shares of TC for $67 million, or $1.67/share. Carrying value of TCI shares at September 30 was $0.629/share ($214 million / 340.3 million shares). Fairfax should book a benefit of about $42 million when it reports Q4 results.

Fairfax Gain on Sale on Thomas Cook India Shares
December 1, 2023

Sale Price	Carrying Value	Gain /Share	Shares Sold	Total Gain
US$	US$	US$	mn	US$ mn
$1.675	$0.629	$1.046	40	$42

Background on Fairfax's additional investment in TCIL in 2021

In 2021, TCIL needed some cash to help it get through Covid and Fairfax stepped up with a $60 million preferred share investment. At the time, I am sure a lot of Fairfax investors questioned what the company was doing - was this an example of Fairfax throwing good money after bad? Of doubling down yet again on a bad business? Investors who thought this were wrong. Very wrong.

On its $60 million additional investment in TCIL in 2021, Fairfax is up about $104 million or 173% over the past 2.5 years. That is a terrific return.

Fairfax's Return on $60 mn Capital Injection to TCIL During Covid					
US$		**Amount US$ mn**	**Shares mn**	**Amount per share**	
2021 & 2022	Investment	$60	92.1	$0.65	
Dec 1, 2023	Sale	$67	40.0	$1.675	
Dec 4, 2023	Balance	$97	52.1	$1.86	
US$		**Value**	**Cost**	**Gain**	**%**
Dec 4, 2023	Total	$164	$60	$104	173%

It was an opportunistic deal for Fairfax. But also, much needed at the time by TCIL.

"During 2021, Thomas Cook India raised $60 million from Fairfax through optionally convertible redeemable preference shares with a 10.7% dividend yield, a seven-year tenure and an option to convert into ordinary shares of the company at 47.30 rupees per share within 18 months from the date of issuance. Thomas Cook India chose to convert the entire amount over two tranches resulting in Fairfax's ownership increasing to 73.3%." *Fairfax 2022AR*

The big picture

The financial benefit for Fairfax of this investment made during Covid goes well beyond the gains from the $60 million capital infusion into TCIL. The investment gave TCIL valuable financial breathing room during Covid and allowed them to right-size their operations - TCI aggressively cut costs. With its travel businesses rebounding strongly in 2023, the much lower cost base is now spiking profits at TCIL.

"Thomas Cook India implemented extensive cost saving initiatives combined with enhanced automation to mitigate the drop in business and improve profitability as normalcy returns. We are pleased to note that total costs were down 40% compared to pre-pandemic levels, while a permanent saving of 20% in overheads compared to the pre-pandemic levels is envisaged."
Prem Watsa – Fairfax 2022AR

Covid also caused Sterling Resorts, owned by TCIL, to lower costs and re-imagine its business model. The results at this subsidiary at TCI have been extraordinary and are another reason profit is spiking at TCIL in 2023.

Comments from Prem about Sterling Resorts from the 2021AR.

> "You will recall from my letter in 2014 that Thomas Cook acquired Sterling Resorts in 2014, mainly because of Ramesh Ramanathan, the CEO of the company. As you can imagine, Sterling faced difficult times in the last two years during the COVID-19-inspired lockdowns. Ramesh did a remarkable job in managing cash flow, allowing the company to stay self-sufficient throughout this period. Also, Ramesh used this time to reorient Sterling's business model and transform it into a holiday experience company." *Prem Watsa – Fairfax 2021AR*

Comments from Prem about Sterling Resorts from the 2022AR.

> "Sterling Resorts, a subsidiary of Thomas Cook India, reported its best ever results, thriving as it remained a premier leisure hospitality brand in India with 39 resorts, 37 destinations and more than 2,300 rooms besides offering vacation time share. You will recall that my letter last year reported on the leadership transition at Sterling, and we are happy to report the smooth transition from Ramesh Ramanathan to Vikram Lalvani, with excellent results achieved at Sterling during the year. Under Vikram's leadership, Sterling emerged out of two years of pandemic with a revival in the resort business in 2022 surpassing the performance of the pre-pandemic period, despite some impact due to the third wave of COVID in Q1, reporting 18% growth in revenue over the year 2019 and 21% over 2021. Its EBITDA of $15 million in 2022 is over fifteen times the $1 million it reported in 2019, and it grew 66% over 2021 on a normalised basis. The operating free cash flow doubled during the period. It ended 2022 with surplus cash and investments of $11 million besides achieving debt reduction of $4 million during the year. Sterling is focused on scaling the resort business by increasing non-member occupancies, boosting revenue from room rates and increasing food and beverage sales. Non-profitable resorts are being dropped from the portfolio, alongside a decreased focus on volume in favour of quality. With the Sterling experience getting appreciation from non-members, the focus is going to be on the quality of growth and enhancing the brand experience at the same time." *Prem Watsa – Fairfax 2022AR*

<u>Fairfax demonstrates it is a very good partner</u>

TCIL is good example of a Fairfax equity holding that was negatively impacted by Covid (BIAL and Recipe are two other Fairfax holdings that were also severely affected by Covid). Fairfax supported the company when times were tough. TCIL got to work and has emerged today stronger (and more profitable) than ever. Fairfax shareholders are now reaping the reward.

An earnings turnaround at equity holdings negatively impacted by Covid is another reason why reported earnings at Fairfax continues to 'surprise' to the upside. A headwind to reported earnings for Fairfax in 2020 and 2021 has now become a tailwind in 2023.

Comments from Prem about Thomas Cook India from the 2022AR.

> "We are happy to note a substantial recovery in Thomas Cook India's businesses during 2022. With excellent leadership by Madhavan Menon, Thomas Cook India exited the year reporting a 90% recovery in its forex business, 79% recovery in its outbound travel business and 84% recovery in its inbound travel business. This is following a difficult year in 2020 when COVID-19 caused its travel business to decline by 90% and its forex business to decline by 75%, and an incipient recovery of 53% in forex business and 27% in travel business in 2021. Business recovery combined with cost reductions resulted in its results improving – a pre-tax loss of $2 million in 2022 compared to a pre-tax loss of $46 million in 2021." *Prem Watsa – Fairfax 2022AR*

Below is a brief history of Fairfax's investment in Thomas Cook India:

TCIL was Fairfax's first large purchase in India. In 2012, Fairfax purchased 87.1% for $173 million. TCIL subsequently made three large acquisitions to round out its portfolio of assets:

- Feb 2014: Sterling Resorts for $140 million plus shares (Fairfax invested $81 million).
- Aug 2015: Kuoni India and Kuoni Hong Kong for $64 million
- March 2019: Digiphoto Entertainment Imaging (51% interest) for $21 million.

Comments from Prem about Thomas Cook India from the 2020AR.

> "As you will recall, our first major acquisition in India was the purchase of a 77% interest (later reduced to 67%) in Thomas Cook India, led by Madhavan Menon. Thomas Cook, first set up in India in 1881, is the leading integrated travel and travel-related financial services company in India, offering, through its 4,700 employees, a broad spectrum of services that include foreign exchange, corporate travel, leisure travel, insurance, visa and passport services and e-business. With the 2015 purchase of Kuoni's Indian travel business and then its operations all over the world, Thomas Cook India is today one of the largest high-end travel service provider networks headquartered in the Asia-Pacific region. With the 2019 purchase of Digiphoto Entertainment Imaging ("DEI"), Thomas Cook has emerged as a complete travel solutions company. DEI provides imaging solutions for the entertainment industry, giving Thomas Cook India an opportunity to package DEI products with Thomas Cook Tours. Established in 2004, DEI has offices throughout the Far East, as well as in the Middle East, India and the U.S., and has a network of 130 entertainment partners." *Fairfax 2020AR*

The IKYA/Quess Home Run

In 2012, Fairfax designated TCIL as the vehicle through which it was going to be investing in India. In May of 2013, TCIL purchased a 77.3% interest in IKYA (renamed Quess) for $47 million. In 2017, TCIL sold 5.4% of Quess for $97 million. In December 2019, TCIL spun out all of Quess. Fairfax currently owns of 35% of Quess. IKYA/Quess has been a very good investment in India for Fairfax.

Strategic Shift

Modi's election in 2014 caused Fairfax to shift its strategy in India. Fairfax wanted to accelerate its investments and TCIL's structure was too limiting. In 2015, Fairfax India was born and it was decided this platform would house all of Fairfax's future non-insurance investments in India. However, legacy investments like TCIL and Quess would continue to be owned directly by Fairfax. Fairfax also owns Digit directly - its insurance vehicle in India.

A short summary of Fairfax's ownership of TCIL shares

Change in Fairfax's Ownership In Thomas Cook India			
	Shares		
	mn	%	
Dec 31, 2020	248.2	66.8%	
Dec 31, 2022	340.3	72.3%	Acquired 92.1 million shares at INR 47.3
Dec 1, 2023	300.3	63.8%	Sold 40 million shares at INR 140

Private Equity Holdings

- AGT Food and Ingredients
- Recipe

AGT Food and Ingredients

Feb 11, 2024

Murad Al-Katib, President and Chief Executive Officer - AGT Food and Ingredients Inc.

On September 19, 2023, Murad gave a 75 minute talk to his Alma Mater, Edwards School of Business in Saskatoon, Saskatchewan.

Click the link to watch the YouTube video:
- https://youtu.be/DzE9ypecdI8?si=cxvsU3EeXoXGzELc

AGT reported Sales in 2022 = C$2.8 billion (the slide below is from the video)
In Fairfax's 2022AR, Prem said AGT had EBITDA of C$150 million

AGT Food and Ingredients

July 31, 2023

AGT is a sleeper holding for Fairfax. It is a private holding so the information on it available to shareholders is scarce. Fairfax owns about 60% of the company. EBITDA was C$150 million in 2022, up from C60 million four years ago.

Who is AGT Food Ingredients?

From the Company's Web Site: http://www.agtfoods.com

"AGT Food and Ingredients is one of the largest suppliers of value-added pulses, staple foods and food ingredients in the world. We buy lentils, peas, beans and chickpeas from farmers around our 40+ facilities located in the best pulse growing regions in Canada, the United States, Turkey, Australia, China and South Africa and ship our products to over 120 countries around the globe. We create value for producers, quality products for our customers and growth for our stakeholders."

Comments from Prem about AGT from the 2022AR.

"AGT, run by founder and CEO Murad Al-Katib, had a record year in 2022, with EBITDA of over Cdn$150 million. This is a dramatic improvement from the time of the take-private transaction almost four years ago when the business was generating slightly over Cdn$60 million in EBITDA. This growth in EBITDA was driven by strong processing margins as the global market for pulses (beans, lentils and peas) has continued to normalize after the initial disruption of import tariffs being implemented by the world's largest consumer of pulses, India. AGT also had stronger profitability in its expanding bulk handling and packaged foods and ingredients segments and is a key supplier for global humanitarian programs in Ukraine, Syria and Afghanistan and famine relief programs for the Horn of Africa. One of AGT's largest processing facilities is located in Mersin, Turkey. While staff and the plant itself were not harmed, we are deeply saddened by the tragedy caused by the earthquakes in southern Turkey. AGT has committed to use its extensive infrastructure to help in the relief efforts. Fairfax has an approximate 60% stake in AGT and we are excited by the ever increasing plant-based applications in everyday food and by AGT's growing pasta business."
Prem Watsa – Fairfax 2022AR

Recipe – A Deep Dive

April 18, 2023

I am warming up to Fairfax's recent take-private deal for Recipe. Recipe WAS a terrible investment for minority shareholders forever. However, what investors in Fairfax care about today is how will the company perform for Fairfax moving forward? How much cash flow will Recipe be able to deliver each year moving forward? I think it will be able to get back to historical free cash flow levels of around C$130 million (US$95 million) per year to Fairfax (their 84% share). This earnings stream should also be pretty consistent year in year out and should grow nicely over time.

In the near term I am interested to see what Recipe does with their free cash flow. We now know US$100 million of the US$340 million purchase price was funded by an increase in debt at Recipe. So perhaps free cash flow at Recipe in the near term will be used to pay down this additional debt. Longer term it will be interesting to see if Recipe uses free cash flow to expand (likely US) or if they pay it out to Fairfax - who then invests it. I am hoping it goes to Fairfax.

Recipe might be a great example of a company that needed to go private to reach its potential. Being a publicly traded company has its weaknesses. Recipe did so many major acquisitions over the past 10 years it likely has some work to do to get systems etc updated and fully integrated and working seamlessly. Fairfax hinted as much as a reason for the take private deal. Recipe also has some hidden assets like real estate. Bottom line, Fairfax was likely very opportunistic with this purchase.

The minority shareholders were the ones left holding the bag. As a reminder, Fairfax paid C$20.73 for the shares in Recipe it did not own. Here are the capital raises done by CARA/Recipe over the years:

- 2015: CARA IPO C$230 raised at C$23/share
- 2015: Phelon family sells $103 million at C$37.75/share
- 2016: capital raise to fund St Hubert: C$230 million at C$29.25
- 2018: capital raise to fund Keg: C$95 million at C$24.93

For those who want more history on Recipe, below is a post from last year.

September 5, 2022

What follows is a very long post… everything you wanted to know about Recipe and Fairfax. On Sept 1, 2022, Recipe agreed to be taken private by Fairfax. Shareholder approval should come in Q4. The cost to Fairfax? C$465 million = US$354 million. Fairfax will own 84% and Cara Holdings (founding Phelan family) will own 16%.

Ownership after take-private:

- Cara Holdings (Phelan) 9.4 million
- Fairfax currently 27.0 million
- Fairfax to buy 22.4 million at C$20.73 = C$465 million
- Total shares outstanding 58.8 million at C$20.73 = C$1.22 billion market cap
- Total net debt C$340 million; Enterprise value = C$1.56billion

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Why is Fairfax doing this? Fairfax sees Recipe shares as being significantly undervalued at C$20.73.

Is Fairfax right? The problem is covid has wreaked havoc on results of restaurant operators in Canada since Q1, 2020, especially full service dine-in restaurants (the largest portion of Recipe's restaurant count). Repeatedly locking down an economy is not good for business, especially for restaurants. So, looking at Recipe's financial results the past 10 quarters is not very helpful.

What about going back 2017 to 2019? Free cash flow (before growth capex, dividends, and NCIB) at Recipe was:

- 2017 = C$144 million
- 2018 = C$164 million
- 2019 = C$156 million

Clearly, Fairfax expects Recipe - in the coming year or two - to get back to a run rate of around C$150 million in free cash flow. If this happens then this will become a very good purchase for Fairfax shareholders. The earnings from Recipe, while cyclical, should also be relatively consistent year to year providing some stability and important diversification from Fairfax's other large equity holdings and its insurance business.

What is Fairfax's total lifetime cost for 84% of Recipe?

My guess is US$354 + $348 = $702 million

I base my above estimate on two data points:

1. Cost to Fairfax to take out minority shareholders of US$354.
   - 22.4 million share x C$20.73 = C$465 million

2. Total $ amount Fairfax invested in Prime/Cara/Recipe from 2011 to present to establish their current ownership stake of 46% of $348 million.
   - At the time of The Keg merger with Cara/Recipe in 2018 Fairfax said they had invested a total of $348 million over the years. My guess is Fairfax did not put any more money into Recipe after 2018.

Recipe did pay a quarterly dividend from after the IPO in 2015 until early 2020. It Started at C$0.0917/quarter and finished at C$0.1177

Because Recipe received wage benefits from the government during the pandemic it is not able to pay a dividend until 2023 (if it did it might have to pay back the benefits received from the government during covid). If not for the government restriction I think it is likely Recipe would have reinstated the dividend when Q2 results were released. Instead, Recipe has been using free cash flow to pay down its long-term debt. On Dec 31, 2019 net debt was C$440 million. Q2-2022 net debt was down to C$340 million. I wonder if Fairfax will have Recipe increase long term debt to help fund part of the C$465 million in cash needed in the take private transaction.

Fairfax has been investing in Canadian restaurant stocks since 2011. The Prime Restaurants purchase was the start of a massive consolidation by Fairfax of the full-service restaurant industry in Canada that would culminate in 2018 with the merger of Cara with the Keg (the last large purchase) and the rebranding of the company from Cara to Recipe. Bill Gregson (formerly the CEO of The Brick, a former Fairfax holding), who had led the massive roll up of full-service restaurant banners, retired in 2018 and was replaced by Frank Hennessey, who remains CEO today. Frank's job the past 4 years has been one of digesting all the large acquisitions made the previous years. More recently, we have seen Recipe shedding non-core brands like Milestone's, shedding underperforming locations/franchisees and paying down long-term debt. Today Recipe has more than 1,200 restaurants and is the largest full-service restaurant operator in Canada. The bottom line is Fairfax understands Recipe and the restaurant industry in Canada exceptionally well. Clearly, Fairfax sees a significant value opportunity in taking Recipe private at C$20.73/share.

Much can be learned about Fairfax by looking at its involvement the past 11 years in Prime/Cara/Recipe. Long term focus (a vision to consolidate the restaurant business in Canada). Build long term relationship with equity partner (the Phelon family since 2013 and continuing post take-private). Missteps (Cara overpays on acquisitions). Persistence (multiple, large acquisitions over more than a decade). Adversity (covid from 2020 to 2022). Very opportunistic - minority shareholders beware (take private Sept 2022).

<u>Fairfax began investing in Canadian restaurant stocks in 2011 with two separate purchases.</u>

In Dec 2011 Fairfax invested US$10 million in Imvescor Restaurant Group's recapitalization.

Imvescor banners: Baton Rouge, Pizza Delight, Scores, Toujours Mikes, Ben & Florentine. Fairfax added to their position in Nov 2012 ($1 million) and then sold their entire position to GMP Securities in April 2013 for proceeds of $26 million.

The second purchase was the start of an 11-year journey with many twists and turns that is now culminating in Fairfax's C$1.2 billion take private offer for Recipe.

1.) Initial purchase: In Nov 2011, Fairfax outbid Cara (oh, the irony) and purchased 81.7% of Prime Restaurants (East Side Mario's, Casey's, Prime Pubs and Bier Markt) for US$69 million.

2.) Cara merger: Oct 2013 Prime was merged with Cara Operations (Swiss Chalet, Harvey's, Milestones, Montana's and Kelsey's). Bill Gregson named CEO. Fairfax invested a total of US$157 million (including its stake in Prime) and owned 49% of Cara which was privately held at the time (Phelan family owned 51%). "Cara has solidified its position as Canada's largest full-service restaurant company with iconic brands that deliver unique dining experiences for Canadians coast to coast. This combined family of restaurants significantly increases Cara's scale, strengthens its market position, and provides opportunities for growth and acquisitions."

3.) Dec 2014: Cara buys majority ownership (55%) in Landing Group, Southern Ontario based, high-volume, upscale casual restaurant concept. Remaining 45% ownership was purchased June 2015.

4.) Cara IPO: April 2015, Cara went public. Post IPO, Fairfax owned 40.7% (53.2% voting control) and Cara was debt free. IPO raised raised C$230.1 million (US$180) = 10 million shares @ C$23/share (including over-allotment). I think this is when Fairfax obtained voting control of Cara from the founding Phelon family. Fairfax would be driving the strategic direction of Cara from this point forward.

5.) Aug 31, 2015: Cara purchases New York Fries. "With 120 locations in Canada and another 36 abroad, New York Fries is one of Canada's most successful QSR concepts." "Cara is acquiring New York Fries for cash consideration which will be funded through Cara's existing credit facilities. The acquisition is accretive for Cara shareholders. The addition of New York Fries also helps diversify Cara's portfolio of stores into shopping centers where Cara's existing 10 brands currently have limited presence."

6.) Dec 2, 2015: Phelan family sells 3 million Cara shares @ $34.75/share (in secondary offering) for C$104 million. Fairfax continues to own 40.5% of shares and now has 57% of voting rights.

7.) Quebec expansion: March 31, 2016, Cara purchases St-Hubert for C$537 million (US$406). "The acquisition provides Cara with a restaurant chain that resonates with guests in Québec as well as with a food retail solution for the Cara brands – these are two areas of Cara's existing business where we have tremendous opportunities. It also provides Cara with a head office in Québec, manufacturing facilities, and a skilled management team that will grow and manage the Cara Québec restaurant expansion and national retail food initiative." Includes a valuable real estate portfolio consisting of 28 owned properties including 2 manufacturing plants. St-Hubert generated approximately $620 million in System Sales, including the food operations division, and approximately $44.8 million in Operating EBITDA.

8.) To fund St-Hubert acquisition, Cara raises C$230 million (US$174 million) = C$29.25 x 7.86 million shares. Fairfax purchases 3.487 million shares for C$102 million (44% of newly issued shares).

9.) West expansion: Sept 1, 2016: Cara purchases Original Joe's for C$93 million (US $70) - Original Joe's Restaurant & Bar, State & Main Kitchen Bar and Elephant & Castle Pub and Restaurant. "With its proven restaurant-pub concepts and its understanding of the casual, full-service foodservice space, Original Joe's is a natural fit for Cara. The majority of Original Joe's restaurants are located in Western Canada, an area where Cara is currently under-represented." "Original Joe's 99 restaurants generate approximately $250 million in annual System Sales and approximately $14.7 million in Normalized Operating EBITDA before synergies."

10.) Last big acquisition: Feb 2018, The Keg merged with Cara. Cara pays C$200 million (US$154) = C$105 million in cash and C$95 million in shares = 3.8 million new shares issued at @ C$24.93. Cara changes name to Recipe

- Fairfax 51% interest in Keg sold to Recipe for $7.9 million + 3.4 million Recipe shares (Fairfax ownership of Recipe = 43.2%)
- Total Fairfax investment to date in Cara = $348 million

11.) April 30, 2018: Frank Hennessey appointed CEO of Cara. Bill Gregson steps down as CEO to become Executive Chairman of the Board.

12.) Oct 24, 2019: after additional C$4 million purchase, Recipe owns a total of 29.15% of units in Keg Royalties Income Fund (traded on TSX)

13.) Dec 10, 2019: Bill Gregson retires as Executive Chairman of the Board of Recipe Unlimited. Paul Rivett, President of Fairfax Financial Holdings Limited, will assume the role as Chairman of the Board of Recipe Unlimited. Mr. Gregson commented, "Thanks to the hard work of all our amazing teammates and franchisees, we have built a business that today generates $3.5 billion in system sales and over $200 million in EBITDA. Today, the company has a strong balance sheet and a solid business process foundation. Now with the CEO transition to Frank Hennessey complete, the company is planning its next evolution to prosper in an ever-changing world.

14.) May 6, 2021: Recipe completed the acquisition of Crave It Restaurant Group's ("Crave It") ownership interest in both The Burger's Priest and the 'Fresh – Crave It – Recipe' joint venture for new market growth of Fresh Plant Powered ("Fresh Restaurants"). "Both The Burgers Priest and Fresh Restaurants are dynamic omni-channel brands that have very loyal customer followings. Recipe is excited about the future potential of these dynamic brands."

About Recipe: Founded in 1883, Recipe Unlimited Corporation (formerly Cara Operations) is Canada's oldest and largest full-service restaurant company. The Company franchises and/or operates some of the most recognized brands in the country including Swiss Chalet, Harvey's, St-Hubert, The Keg, Montana's, Kelsey's, East Side Mario's, New York Fries, Prime Pubs, Bier Markt, Landing, Original Joe's, State & Main, Elephant & Castle, The Burger's Priest, The Pickle Barrel, Marigolds & Onions, and 1909 Taverne Moderne.

Other Equity Holdings

BDT & MSD Partners

October 2023

Who is BDT?

BDT is a high quality merchant bank focused on serving the needs of privately held, family run businesses across the world.

"BDT & MSD Partners is a merchant bank with an advisory and investment platform built to serve the distinct needs of business owners and strategic, long-term investors. We are distinguished by our decades of experience advising at the intersection of founders, families, and businesses, as well as by our differentiated capital base and culture of aligned investing. Since 2010, our affiliated funds have deployed more than $50 billion across our investment strategies." *https://bdtmsd.com*

What is Fairfax's investment in BDT?

In the 2022AR, Prem said Fairfax's investment in BDT had a market value of $508 million. At the time, this was Fairfax's 7th largest equity holding by size (representing about 3.4% of Fairfax's total equity portfolio of $14.9 billion).

Comments from Prem about BDT from the 2022AR.

"We continue to invest with Byron Trott through various BDT Capital funds. Since 2009, we have invested $772 million, have received $960 million in distributions and still have investments with a year-end market value of $508 million. Byron and his team have generated fantastic long-term returns for Fairfax, and we very much look forward to our continued partnership." *Fairfax 2022AR*

Additional information on Byron Trott, CEO of BDT

Of interest, one of Brian Trott's mentors was Warren Buffett (he mentions this in the video).

University of Chicago Booth School of Business: Distinguished Speaker Series
- May 28, 2020
- YouTube video (59 minutes)

Byron Trott - chairman and CEO, BDT Capital Partners

Summary: Byron speaks about his 27-year career at Goldman Sachs and his experience founding his own firm, BDT Capital Partners on May 26, 2020.

https://youtu.be/DsQ7NkMUCSE?si=SS3vjqponBGrtb9_

Chapter 12: Geographies

One of the things that separates Fairfax from many peers is its significant international insurance operations. Fairfax also has extensive international investments. After the US and Canada, India and Greece are the two most important countries for Fairfax.

India – So Many Tailwinds

May 23, 2023

After the US and Canada, India is Fairfax's most important geography. In a world starved for growth, India is expected to be one of the fastest growing economies over the next decade. Morgan Stanley is projecting an economic boom in India (see below). Fairfax has repeatedly said they believe India is best country to invest in today. So, we should expect India to increase in importance for Fairfax investors in the coming years.

Below is a bit of a deep dive on India and Fairfax:

1. India: the big picture

I will then zoom into Fairfax and India

2. Summary of current investments in India
3. History: Insurance investments
4. History: Non-insurance investments
5. People
6. Summary

1.) India: the big picture

India is exceptionally well positioned today:

- demographic tailwind: India has the largest population in the world, and it is very young with a median age of 28.2 years (China's is 39). This should drive higher domestic consumption.
- regulatory tailwind: India has a pro-business government - ease of doing business in India is improving greatly. This should drive investment spending.
- geopolitical tailwind: companies are aggressively looking to diversify supply chains away from China - Apple's plans to shift 25% of iPhone production to India in just one recent example.

Many important building blocks are in place. This should result in strong economic growth for India over the next decade. India looks positioned to finally realize its vast potential - it is no longer just a dream.

Below is a link to a report on India from Morgan Stanley.

India's Impending Economic Boom: India is on track to become the world's third largest economy by 2027, surpassing Japan and Germany, and have the third largest stock market by 2030, thanks to global trends and key investments the country has made in technology and energy.

https://www.morganstanley.com/ideas/investment-opportunities-in-india

The following video was mentioned by Prem in his letter in Fairfax's 2022AR.

The Future of India: Deepak Bagla, Managing Director & CEO, Invest India

https://www.youtube.com/watch?v=45PrXujlQCo

2.) Summary of Fairfax's current investments in India

Fairfax's business model has much more of an international focus than most of its P/C insurance peers. This is true for both insurance and non-insurance investments.

Fairfax does a good job of summarizing for shareholders all their investments in India each year in the annual report. Below is the summary provided in the 2022AR. Key take-aways:

- Insurance investments (Digit) fair value = $2.3 billion
- Non-insurance investments fair value = $1.5 billion

Fairfax has a total of about $15 billion in equity investments. On December 31, 2022, non-insurance investments in India of $1.5 billion represented about 10% of Fairfax's total.

	Date of Initial Investment	Ownership	Cost	Fair Value at December 31, 2022	Compound Annualized Return
Thomas Cook India	Aug-12	73.3%	315	293	10.7%(1)
Fairfax India	Jan-15	41.6%	534	703	4.3%
Digit	Feb-17	49.0%	154	2,278	79.5%
Quess	Dec-19	30.1%	335(2)	222	(7.1)%
Other			365	308	
			1,703	3,804	
Fairfax India's investments					
Bangalore International Airport	Mar-17	54.0%	653	1,234	12.2%
IIFL companies(3)	Dec-15		156	634	19.8%
Sanmar Chemicals	Apr-16	42.9%	199	338	13.2%
CSB Bank	Oct-18	49.7%	170	223	7.5%
Seven Islands	Mar-19	48.5%	84	97	4.0%
NCML	Aug-15	89.5%	188	69	(13.8)%
Fairchem Organics	Feb-16	52.8%	30	111	34.1%
National Stock Exchange	Jul-16	1.0%	27	160	35.2%
Saurashtra Freight	Feb-17	51.0%	30	51	10.1%
Maxop	Nov-21	67.0%	51	52	0.8%
Jaynix	Feb-22	70.0%	32	33	1.0%
Other			34	38	24.8%
			1,654	3,040	13.2%

(1) Includes dividends received ($11 million) and spinoff of Quess ($330 million)
(2) Cost shown for Quess represents its market value on December 5, 2019, the date it was spun off from Thomas Cook India
(3) IIFL companies include IIFL Finance, IIFL Securities, 360 ONE WAM (formerly IIFL Wealth) and 5paisa

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3.) A short history of Fairfax's insurance investments in India

Fairfax began its insurance journey in India in 2000. That was the year the government in India opened the property and casualty insurance industry to foreign investment. Fairfax partnered with ICICI Bank, a large private bank in India, and created a joint venture called ICICI-Lombard. Fairfax invested $10 million for an interest of 26% in the new venture, the maximum allowed by Indian law at the time.

ICICI-Lombard experienced rapid growth in the years that followed and by 2006, they had become the largest private general insurance company in India with a 12.5% market share. Over the years Fairfax made numerous capital infusions to support the growth of ICICI-Lombard and maintain their ownership at 26%.

In 2015, the Indian government allowed foreign ownership in insurance companies to increase to 49%. That year Fairfax purchased an additional stake of 9% in ICICI-Lombard from ICICI Bank for $234 million; this increased Fairfax's ownership in ICICI-Lombard to 35%.

In 2017, ICICI Bank decided it was time to take ICICI-Lombard public. ICICI Bank wanted to maintain ownership of at least 55% (to maintain control). Indian law required the public to own at least 25% of an IPO. This meant Fairfax would need to reduce its position to a 'mere' 20%.

Solution? Fairfax decided it was time to start their own P/C insurer in India. So, they partnered with Kamesh Goyal and brought start-up Digit into the Fairfax family. What a gutsy call this was at the time.

Indian law does not permit ownership of 10% or greater in more than one insurance company so an agreement was struck with ICICI Bank for Fairfax to reduce their interest in ICICI-Lombard to below 10%. In 2017, Fairfax reduced their equity interest in ICICI-Lombard from 35% to 9.9% and booked an after-tax gain of $930 million. Fairfax sold their remaining position in ICICI-Lombard in 2019 for $729 million and booked another $311 million gain. My guess is Fairfax earned more than $1.15 billion after-tax from its 20-year investment in ICICI-Lombard. Impressive value creation for shareholders.

Digit is now the property and casualty insurance engine for Fairfax in India. Growth has been rapid. In 2019, three private equity firms purchased 10% of Digit for $91 million; this valued the company at $858 million. In 2021, Digit raised another $200 million; this capital-raise valued the company at $3.5 billion. In 2021, Fairfax recorded a net unrealized gain of $1.4 billion on its investment in Digit compulsory convertible preferred shares (CCPS). Additionally, "The company anticipates recording additional gains of approximately $400 upon consolidating its investment in Digit, which is subject to regulatory approvals permitting the company to increase its 49.0% equity interest in Digit to a control position." Fairfax is still waiting for final approval from Indian regulators (yes, this is understated… buy I am trying to keep this summary short).

From Prem's Letter in the 2022AR: "Digit, led by Kamesh Goyal, had another strong year: after only five years since its inception, premiums are over $900 million, up 50% over the last 12 months in local currency, and with the benefit of investment income it had another profitable year. Digit entered the Fortune India magazine's ranking of India's 500 largest companies by total revenue during the year at 398th on the list – we expect that will move up going forward! Digit is exploring an IPO in 2023 which would fund future growth."

On December 31, 2022, Digit had a cost of $154 million and a fair value of $2.28 billion = a compound annualized return of 79.5%. Fairfax looks exceptionally well positioned to grow in insurance in India with Digit.

4.) A short history of Fairfax's non-insurance investments in India

Fairfax's first large non-insurance investment in India was Thomas Cook India in 2012. Modi's election in 2014 led to Fairfax's next big move - the creation of Fairfax India in 2015. As a result, we are going to split this short history into two buckets: Thomas Cook India and Fairfax India.

Thomas Cook India

In 2012 Fairfax purchased 87.1% of Thomas Cook India (TCI) for $172.7 million. This was Fairfax's largest single purchase in India and the start of much more to come. At that time, Thomas Cook was designated the vehicle for Fairfax's future non-insurance investments in India.

- In early 2013, TCI purchased 74% of IKYA - renamed Quess - (Founder CEO - Ajit Isaac) for $47 million.
- In 2014, TCI purchased Sterling Resorts for $140 million.
- In 2015, TCI purchased Kuoni India for $32.5 million and Kuoni Hong Kong for $47.9mn.

In 2017, Thomas Cook India sold 5.4% of Quess for $97 million. Thomas Cook India completed its spin-off of Quess (which became a stand-alone company) in December of 2019. Fairfax's direct ownership in Quess was 32% (in Dec 2019: cost = $33 million; market value = $332 million; carrying value = $704 million).

Prime Minister Narendra Modi's election in 2014 caused an important change in Fairfax's strategy with its investments in India. Given Modi's election, and expected business friendly policies, Fairfax decided to accelerate the pace of its investing in India. However, Thomas Cook India's resources were a constraint on that growth. What to do? Fairfax made a significant pivot and decided to launch Fairfax India.

Comments from Prem about Prime Minister Modi from the 2014AR.

"Mr. Modi's election led us to rethink the investment opportunities in India and our ability to fund them. While we have $26 billion in investments at Fairfax, regulatory constraints limit our ability to invest significant amounts in India. Given our excellent long term track record investing in India, our very significant on the ground resources with Harsha Raghavan at Fairbridge, Madhavan Menon at Thomas Cook India, Ajit Isaac at Quess (the new name for IKYA), Ramesh Ramanathan at Sterling Resorts and also S. Gopalakrishnan, the long serving head of investments at ICICI Lombard, we felt it was appropriate to create a new public company, Fairfax India, to invest in India." *Prem Watsa – Fairfax 2014AR*

Fairfax India

In 2015, the Fairfax India IPO raised $1.1 billion, $300 million from Fairfax (28% equity ownership and 95% of voting control at inception). In 2017, Fairfax India raised an additional $500 million; Fairfax participated and owned 30.1% of equity interest and 93.6% of the voting rights. Today, Fairfax owns 41.9% of Fairfax India.

Company Profile: "Fairfax India Holdings Corporation is an investment holding company publicly traded on the Toronto Stock Exchange whose investment objective is to achieve long-term capital appreciation, while preserving capital, by investing in public and private equity securities and debt instruments in India and Indian businesses or other businesses with customers, suppliers or business primarily conducted in, or dependent on, India."

Overview of Fairfax India - powerpoint presentation from AGM on April 20, 2023

https://s1.q4cdn.com/293822657/files/doc_presentations/2023/Fairfax-India-AGM-2023.pdf

Comments from Prem about Fairfax India from the 2022AR.

"Since Fairfax India began, it has completed investments in 12 companies and exited one (14 currently as one has been split into four listed entities), all sourced and reviewed by Fairbridge, Fairfax's wholly owned sub-advisor in India. Fairbridge does outstanding work under the excellent leadership of CEO Sumit Maheshwari, supported by its Director Anish Thurthi, Vice President Sheetal Sancheti and analysts Jinesh Rambhia, Ramin Irani and Chinar Mathur. Fairfax India's Mauritius subsidiary, FIH Mauritius Investments, ably led by its CEO Amy Tan, supported by its Vice President Vishal Mungur and its independent Board of Directors, is an integral part of the investment process. Also, since Fairfax India began, Deepak Parekh, both as a trusted advisor and a member of the Board of Directors, has provided us with invaluable advice on almost all of its transactions."

"All of Fairfax India's investments are in outstanding companies with a history of strong financial performance, led by founders and management who are not only excellent but also adhere to the highest ethical standards." *Prem Watsa – Fairfax 2022AR*

Bangalore International Airport Limited (BIAL)

Fairfax's India's largest and most important investment is Bangalore International Airport Limited (BIAL). At December 31 2022, Fairfax had invested a total $653 million in BIAL which at that date had a fair value of $1.2 billion. Fairfax India just announced an additional purchase of 3% of BIAL from Siemens for $75 million and agreed to acquire an additional 7% later in 2023 (taking their ownership to 64%) for $175 million. This would take Fairfax India's ownership in BIAL to 64%.

Comments from Prem about BIAL from the 2022AR.

"As I have said many times in past annual reports, the crown jewel (and largest) of Fairfax India's investments is the Bangalore International Airport, run by Hari Marar. In 2022, Hari and his team did the impossible – they built the most beautiful airport in the world (Terminal 2 or T2) in a record four years, of which two were interrupted by COVID! In my mind, there is no airport in the world like T2 and it will be an inspiration for travellers arriving in Bangalore, the state of Karnataka and India. It will show the world anything is possible in India." *Prem Watsa – Fairfax 2022AR*

Fairfax India's performance:

Here is a snapshot of Fairfax India's performance since it began:

$ millions except per share amounts:	2022	2021	2020	2019	2018	2017	2016	2015	CAGR[(1)]
Book value per share	$ 19.11	$ 19.65	$ 16.37	$ 16.89	$ 13.86	$ 14.46	$ 10.25	$ 9.50	8.5%
Income	237.5	693.5	(13.0)	712.7	166.5	609.7	128.6	65.3	
Net earnings (loss)	191.4	494.5	(41.5)	516.3	96.4	452.5	107.8	40.9	
Return on equity	7.1%	18.9%	(1.7)%	22.0%	4.5%	28.2%	10.3%	4.0%	11.7%[(2)]
$ billions:									
Total assets	3.4	3.6	3.1	3.2	2.7	2.7	1.3	1.0	16.2%
Investments	3.2	3.5	3.0	3.2	2.7	2.6	1.1	1.0	16.2%
Common shareholders' equity	2.6	2.8	2.4	2.6	2.1	2.1	1.1	1.0	12.9%
Shares outstanding (millions)	138.3	141.2	149.5	152.6	152.9	147.4	104.9	106.7	

(1) Since Fairfax India's inception on January 30, 2015, when it raised $1.03 billion at $10 per share. From an initial value of $9.62 (after IPO expenses), book value per share has compounded at 9.0% annually.

(2) Simple average of the return on equity for each of the eight years.

Fairfax India's Anchorage IPO:

Comments from Fairfax India about Anchorage from the 2022AR.

"In June 2019, Fairfax India created a 100% owned subsidiary in India named Anchorage Infrastructure Investments Holdings (Anchorage). It is intended that this company will be Fairfax India's flagship investment vehicle for airports and other infrastructure investments in India and that all the shares it owns in Bangalore International Airport (BIAL) will eventually be transferred to Anchorage.

"In September 2021, Fairfax India, as previously agreed, transferred 43.6% out of the 54% that it owns in BIAL to Anchorage and OMERS (the pension plan for municipal employees in the Province of Ontario, Canada) invested $129.2 million to acquire from Fairfax India an 11.5% interest on a fully diluted basis in Anchorage. This resulted in OMERS indirectly owning approximately 5% of BIAL. At that time, this transaction valued 100% of BIAL at $2.6 billion.

"Fairfax India intends to complete an IPO of Anchorage, although we did not move forward on this in 2022 as we are awaiting regulatory approvals.

"Once Anchorage is listed, the proportion of the publicly listed investments in Fairfax India will increase from the current 39.2% to 79.8% of the overall portfolio." *Fairfax India 2022AR*

Summary

Over the past 11 years, Fairfax has dramatically increased the number and size of its equity investments in India. It holds some of these investments directly. More recent investments are held primarily though Fairfax India, of which BIAL is the largest single holding. Anchorage is poised to be a growth vehicle for Fairfax India in the coming years.

Fairfax and Fairfax India's history: link to press releases of most transactions in India

https://fairbridgecapital.com/history.html

5.) People

The CEO of Fairfax, Prem Watsa, was born and raised in India. Since at least 1995, Fairfax has had important resources allocated to India. In 2011, this commitment increased with the creation of Fairbridge Capital which provides Fairfax with significant boots-on-the-ground resources in India.

Chandran Ratnaswami

Chandran is one of the true heroes of this story. He was hired by Fairfax in 1995. Currently a Senior Managing Director at Hamblin Watsa (responsible for East Asia), he is also CEO of Fairfax India. His fingers are all over Fairfax's investments in India for the past 28 years.

Comments from Prem about Chandran from Fairfax's 2017AR.

"In 1995, Chandran Ratnaswami joined us to build our international insurance and common stock investments, particularly in India. I said then, "this may be an acorn for a future oak tree." Well what an oak tree Chandran has developed! We, with ICICI Bank, created the largest non-government-owned property and casualty insurance company in India from scratch, managed an Indian investment portfolio with outstanding results for over 20 years, created Fairbridge with Harsha Raghavan as Managing Director, acquired a 77% interest in Thomas Cook India which then acquired Quess and Sterling Resorts, and finally created Fairfax India which now has a market value of $2.5 billion. Chandran was intimately involved with all of these activities and serves on most of the Boards of our Indian companies." *Prem Watsa – Fairfax 2017AR*

Fairbridge Capital:

Established in 2011, Fairbridge is a subsidiary of Hamblin Watsa that researches and advises on Fairfax's and Fairfax India's investments in India.

From the Fairbridge Capital web site: https://fairbridgecapital.com

"Fairbridge takes a long-term value approach towards acquisitions and investments in the Indian region. We focus on long-term capital appreciation through a flexible and value-oriented approach, underpinned by our guiding principles, including integrity, transparency and responsiveness in all our dealings. Our permanent capital base enables us to execute unique set of transactions; by taking a very long-term view, combined with the ability to execute highly flexible and creative deal structures."

Fairfax also leverages the knowledge and expertise of the various founder/CEO's of the companies it controls in India, like Thomas Cook (Madhaven Menon), Quess (Ajit Isaac) and others.

Fairfax has been building out its 'people' capabilities in India for decades. Most importantly, it has a dedicated team, Fairbridge Capital, with deep local knowledge that can act as opportunities present themselves.

6.) Summary

<u>Fairfax's investing strategy in India</u>:

- Insurance: all insurance investments will be held at Fairfax.
- Legacy non-insurance investments, Thomas Cook and Quess, will remain at Fairfax.
- Most new non-insurance investments will be held at Fairfax India.

<u>What have we learned about Fairfax and India?</u>

- deep understanding of the country
- government deregulation is a significant driver of opportunity.
- partner with strong founder/owners
- decentralized ownership structure
- supportive / very good partner
- long term focus
- strategic
- adaptive
- opportunistic
- entrepreneurial
- diversified

From the very beginning, Fairfax has excelled with both its insurance and non-insurance investments in India. This success is due primarily to the people talent Fairfax has amassed at Hamblin Watsa and Fairbridge Capital. It is like Fairfax has been quietly building out its capabilities in India… preparing and waiting for the right moment… and it appears that right moment may have arrived. If India is the top performing global economy over the next decade, Fairfax certainly looks very well positioned to capitalize on that growth.

"Success occurs when opportunity meets preparation" *Zig Ziglar*

Greece – The Gods Are Smiling

July 28, 2023

Greece has been an interesting geography for Fairfax for the last decade. Fairfax has both insurance and equity investments in Greece. The total value of Fairfax's holdings in Greece is about $3.1 billion. This is made up of equity holdings of $2.655 billion and insurance holdings of about $463 million. Greece is an important jurisdiction for Fairfax.

Over the past couple of years Greece has finally begun emerging from its financial catastrophe. A pro-business government has been busy restructuring the Greek economy. Tourism and property markets are once again doing well. The Greek economy is expected to be one of the top performing economies in Europe in the coming years. The Greek stock market is performing well. The stock prices of both Eurobank and Mytilineos have been on a tear in 2023, with both hitting new multi-year highs recently. Fairfax looks well positioned.

<u>What assets does Fairfax own in Greece today?</u>

- <u>Eurobank</u>: 32.2% ownership of a well-managed bank that includes a very large and profitable property company (formerly Grivalia Properties); its balance sheet appears fixed and 2022 has been a breakout year for profitability. This is the second largest equity holding for Fairfax (based on market value).
- <u>Grivalia Hospitality</u>: 78.4% ownership - deploys capital in the very attractive high-end hospitality sector in Greece and Cypress. Managed by Grivalia Management (also manages real estate holdings for Eurobank).
- <u>Mytilineos</u>: 6.43% ownership (including the exchangeable bond) - a global metallurgy and energy company.
- <u>Praktiker</u>: 100% ownership? A Home Depot type business. Much smaller than the other companies listed above.
- <u>Eurolife</u>: 80% ownership (20% owned by Eurobank). A well-managed insurance company. In 2021, had 31% share of the total life and general insurance market in Greece.

Links to company web sites:

Eurobank:	https://www.eurobank.gr/en/group
Mytilineos:	https://www.mytilineos.gr/who-we-are/mytilineos-company/
Grivalia Hospitality:	https://grivaliahospitality.com/about-us.html
Eurolife:	https://www.eurolife.gr/en

<u>Media Interview with Prem (April 3, 2023)</u>: Greek Banks are Safer

The CEO of Fairfax Financial says Greek banks have up to twice the capital adequacy of the US – 'We are not going to sell a single share'

https://knews.kathimerini.com.cy/en/business/prem-watsa-greek-banks-are-safer

A list of Fairfax's holdings in Greece.

Eurobank is Fairfax's largest single holding in Greece representing 60% of the total.

Date of Initial Investment	Ownership %	Fairfax's Holdings in Greece Equity Holdings	Fair Value 30-Jun (million)	Carrying Value 31-Mar (million)	Shares Owned (million)
2014	32.2%	Eurobank	$1,922	$1,637	1,166
2011	78.4%	Grivalia Hospitality	$409	$409	
2013	4.7%	Mytilineos	$236	$236	6.688
2022	1.8%	Mytilineos Exchange Bond	$88	$88	2.5
2014		Praktiker (not sure of value)	private holding		
	Total Value of Equity Holdings in Greece		$2,655	$2,371	
	Value of Fairfax's Total Equity Holdings		$16,300	Greece + everything else	
	Share of Fairfax's Holdings in Greece		16%		

Date of Initial Investment	Ownership %	Insurance Holdings	Shareholders Equity 31-Dec-22 (million)	
2015	80%	Eurolife - Life Insurance	$393	From 2022 AR
2015	80%	Eurolife - P&C Insurance	$70	From 2022 AR
		Total Insurance Holdings	$463	

A Short History of Fairfax's Investments in Greece

June 2022

Fairfax's 10-year history in Greece has had a couple of triumphs (Grivalia, Eurolife), one catastrophe (initial investment in Eurobank), adversity, heroes, villains, a depression, a pestilence, loyalty, creativity (merger of Grivalia Properties with Eurobank) and years of hard work - it all reads like one of the books of the Iliad by Homer.

Below is a short summary of the odyssey of how Fairfax got to where it is today with its Greek investments. All good stories always start at the beginning. So…

Why did Fairfax invest in Greece?

Answer: Ireland. What?

Fairfax had outstanding success investing in a distressed Irish bank (Bank of Ireland) in late 2011 after the Great Financial Crisis (I think they made +$800 million on this investment - tripled their money in a little over 5 years). And business partner, Kennedy Wilson, had great success investing in real estate in Dublin. So as the cash register was ringing on their Irish investments, Fairfax saw similar opportunities in Greece.

<u>What was the timeline of the Greek purchases?</u>

- <u>2011</u>: purchased 3.8% position in Grivalia (called Europroperties then)
    - Run by George Chryssikos, who is one of the heroes of this story.
    - The Greek journey begins.
- <u>Aug 2012</u>: Grivalia (Eurobank Properties REIT) - Fairfax increased ownership from 3.8 to 18% for $50 million
- <u>2013</u>: Grivalia (Eurobank Properties REIT) - Fairfax increased ownership to 41% for $20 million (plus?)
- <u>Dec 2014</u>: Eurobank: Fairfax makes initial investment of €400 million with group of investors (including Brookfield, Wilbur Ross, Fidelity, Mackenzie, Capital Research and Management)
    - unemployment rate in Greece in 2014 is 28%!
- <u>Nov 2015</u>: Eurobank recapitalization (forced by ECB, one of the villains of our story)
    - Fairfax invests an additional €350 million; ownership increases from 12.5% to 17%. 1 for 100 reverse share split; sold new shares for €1.00.
- <u>Aug 2016</u>: Eurolife: Fairfax purchases 80% ownership; 40% to Fairfax for $181 million and 40% to OMERS for $181 million.
    - purchased from Eurobank. Fairfax was aided in its bid by its ownership in Eurobank (viewed as being good partner); important to Eurobank because the bank was retaining 20% ownership and much of Eurolife's business was transacted through Eurobank distribution channels.
    - referendum in Greece in 2015; Tsipras/Syriza elected; Syria refugees.
- <u>2017</u>: Grivalia - Fairfax Increased ownership to 52.7% for $100 million
- <u>2018</u>: Eurolife - Fairfax increased ownership to 50%; bought 10% from OMERS (whose ownership decreased to 30%)
- <u>Nov 2018</u> (closed May 2019): Eurobank - Fairfax increases stake to 32.4% via merger with Grivalia Properties.
    - all stock transaction valued at US$866 million
    - Fairfax owned 18% Eurobank and 54% of Grivalia; on close Fairfax owned 32.4% of new Eurobank.
    - Grivalia paid €40.5 million special dividend.
    - Eurobank launched property management business run by Grivalia CEO
- <u>July 2021</u> Eurolife: increased ownership to 80% (purchased OMERS 30% stake for $142.6); Eurobank owns remaining 20%
- <u>July 2022</u> Grivalia Hospitality: increased ownership from 33.5% to 78.4% for $195 million; Eurobank owns remaining 21.6%?
- <u>Dec 2022</u> Mytilineos: increased ownership to 4.68% for $53 million

Fairfax's Other Greek investments:

2013 Mytilineos - 5% for €30 million ($41 million)
2014 Praktiker Hellas AE - bought 100% for €21 million.

Why is Eurolife considered a gem?

Comments from Prem about Eurolife from Fairfax's 2019AR.

2019: "Through the crisis in Greece, we acquired a gem in Eurolife, a Greek property and casualty and life insurance company that operates predominantly in Greece but also in Romania. Alex Sarrigeorgiou has run Eurolife since 2004, following Eurobank's decision to grow its insurance business, and we acquired it with OMERS as our partner in 2016. Since our initial 40% purchase of Eurolife in 2016 for €163 million, Eurolife has earned €347 million and paid dividends of €298 million, and shareholders' equity has increased from €400 million to €720 million at the end of 2019 after the payment of dividends. This phenomenal performance was predominantly because Eurolife had a significant holding of Greek government bonds whose rates went from 8% to 1% during that time period while its non-life business had an average combined ratio of 72%. We currently own 50% and equity account for Eurolife but plan to buy the rest of OMERS' shares in 2020."
Prem Watsa – Fairfax 2019AR

2020: "Finally, in Greece, Eurolife has been an extraordinary investment for Fairfax. Writing both Life and Property/Casualty lines, the company in 2020 generated over $500 million of gross premiums written and produced net income of $130 million. Led by Alex Sarrigeorgiou, Eurolife has a track record second to none in the Greek market." *Prem Watsa – Fairfax 2020AR*

2021: "On July 14, 2021 the company increased its interest in Eurolife to 80.0% from 50.0% by exercising a call option valued at $127.3 to acquire the joint venture interest of OMERS for cash consideration of $142.7 (€120.7). The assets, liabilities and results of operations of Eurolife's life insurance business were consolidated in the Life insurance and Run-off reporting segment and those of Eurolife's property and casualty insurance business were consolidated in the Insurance and Reinsurance – Other reporting segment, pursuant to which the company remeasured its 50.0% joint venture interest in Eurolife to its fair value of $450.0 and recorded a net gain of $130.5 in gain on sale and consolidation of insurance subsidiaries in the consolidated statement of earnings, inclusive of foreign currency translation gains that were reclassified from accumulated other comprehensive income (loss) to the consolidated statement of earnings. The remaining 20.0% equity interest in Eurolife continues to be owned by the company's associate Eurobank. Eurolife is a Greek insurer which distributes its life and property and casualty insurance products and services through Eurobank's network and other distribution channels."

(5) "Includes a redemption liability of $124.9 on non-controlling interests as the company's associate Eurobank may put its 20.0% equity interest in Eurolife to the company commencing in 2024 at the then fair value of that interest."

Here is more information on Grivalia Properties which is now part of Eurobank.

Comments from Prem about Grivalia Properties from Fairfax's 2017AR.

"In 2017, we raised our equity interest in Grivalia to 52.7% by buying 10.3% for $100 million when Eurobank decided to divest its interest in Grivalia. It has been six years since we first met George Chryssikos, the outstanding CEO of Grivalia. Through Wade Burton, we took our first position in Grivalia in 2011 at Euro5.77 per share. George has navigated the Greek economic crisis superbly by buying only the highest quality commercial buildings and shopping centres at huge discounts to replacement cost and unlevered returns of 8% to 10%, not using excessive leverage and always focusing on the long term. We are very excited to be partners with George and his team as they build a fantastic real estate company. Like Bill McMorrow at Kennedy Wilson, George has a unique nose for value in real estate! And like all our Fairfax companies, he is building a fine company, focused on its customers, looking after its employees, making a return for shareholders and gratefully reinvesting in the communities where it operates. Business is a good thing!!" *Fairfax 2017AR*

Comments from Prem about the merger of Grivalia Properties into Eurobank in 2019.

"Early in 2019, Fokion Karavias (CEO of Eurobank) and George Chryssikos (CEO of Grivalia) came up with the idea of merging Grivalia into Eurobank, to strengthen the capital position of Eurobank, and accelerating its non-performing loan stock reduction through spinning out €7.5 billion of non-performing loans from the bank to its shareholders. We thought it was a brilliant idea but the process took time as it was subject to shareholder approval at Eurobank and Grivalia and regulatory approval from the ECB. As part of the same plan, Eurobank sold its non-performing loans management unit, FPS, to doValue S.p.A. for €360 million. We expect all these transactions to close by March 31, 2020 and Eurobank to be well capitalized and on its way to earning 10% on its shareholders' equity in 2020. Last year, Greece had an election in which the business friendly party of Kyriakos Mitsotakis won a majority in the parliament. As the new Prime Minister, Kyriakos has the opportunity to transform Greece by encouraging foreign investment into the country and by being business friendly. Ten-year Greek government bonds, which peaked at a yield of 37% in 2012, came down to 10% in 2016 and are now trading below 1%. Recently, Greece did a 15-year bond issue at 1.9% and a 30-year issue at 2.5%. The animal spirits are coming back to Greece and we think the Greek economy and Greek companies will thrive. Eurobank should benefit!! Our cost of 1.2 billion shares of Eurobank after the Grivalia transaction is now 94¢ versus a book value of approximately 135¢ per share post the transaction. At year end, Eurobank was selling at 68% of book value and 6.5x normalized earnings. We still believe it will be a good investment for us." *Prem Watsa – Fairfax 2019AR*

"On May 17, 2019 Grivalia Properties merged into Eurobank, as a result of which shareholders of Grivalia Properties, including the company, received 15.8 newly issued Eurobank shares in exchange for each share of Grivalia Properties. Accordingly, the company deconsolidated Grivalia Properties from the Non-insurance companies reporting segment, recognized a non-cash gain of $171.3 and reduced non-controlling interests by $466.2. In connection with the merger, Grivalia Properties had paid a pre-merger capital dividend of €0.42 per share on February 5, 2019. The company owned approximately 53% of Grivalia Properties and 18% of Eurobank prior to the merger, and owned 32.4% of Eurobank upon completion of the merger." *Fairfax 2019AR*

Chapter 13: Recent Asset Sales

Asset sales are one part of capital allocation that separates Fairfax from its peers. In selling an asset, Fairfax is essentially trading a stream of future cash flows for a lump sum today.

Why sell an asset? Sometimes another company - who is willing to pay up - values an asset at a much higher value than you do. There also can be important strategic reasons to sell an asset. Asset sales have been a very important part of Fairfax's capital allocation framework, realizing significant value for Fairfax and its shareholders over the years.

Ambridge Group – January 2023

May 11, 2023

The sale of Ambridge Group just closed. Proceeds are $400 million (with the opportunity to receive another $100 million subject to 2023 performance targets) and will result in a sizeable realized gain of $275 million for Fairfax. This gain will increase Q2 after-tax earnings by +$10/share.

https://www.fairfax.ca/news/press-releases/press-release-details/2023/Amynta-Group-Completes-the-Acquisition-of-Ambridge-Group-from-Brit-a-subsidiary-of-Fairfax/default.aspx

With the recent closing of both Resolute and Ambridge deals, Fairfax has received proceeds of about $1 billion. This is a significant amount of money. At the same time, Fairfax is also earning a record amount of operating earnings (around $675 million per quarter). It will be interesting to see what new investments Fairfax makes.

The sale of Ambridge is yet another example of Fairfax being opportunistic. This time with the sale of an asset at a premium valuation. Well done.

Brit purchased 50% of Ambridge in 2015 (shortly after Fairfax purchased Brit) for $29 million. Brit purchased the remaining 50% in 2019 for $46.6 million. In 2021, Brit combined their US operations with Ambridge.

Of interest, Fairfax purchased Brit for $1.657 million in 2015. Ambridge is being sold for $400 million (with the opportunity to receive another $100 million subject to 2023 performance targets).

Comments from Fairfax about the Ambridge sale from the 2022AR.

"Sale of Ambridge Group by Brit: "On January 7, 2023 Brit entered into an agreement to sell Ambridge Group, operations, to Amynta Group. The company will receive approximately $400 on closing, comprised principally of cash of $275.0 and a promissory note of approximately $125. An additional $100.0 may be receivable based on 2023 performance targets of Ambridge. Closing of the transaction is subject to customary closing conditions, including regulatory approvals, and is expected to occur in the next few months. On closing of the transaction, the company expects to deconsolidate assets and liabilities with carrying values at December 31, 2022 of approximately $284 and $160, and to record a pre-tax gain of approximately $275 (prior to ascribing any fair value to the additional receivable)." *Fairfax 2022AR*

More historical information about Fairfax and Ambridge.

From Brit 2021 YE Press Release: "In 2021, we combined our US operations to create a single operation under the Ambridge brand. It now operates as a global MGA, managing over $600m of premium in the US and internationally. Our clients have the benefit of the well- recognised Ambridge MGA model giving them better access to products and enhanced service, and our underwriting teams are better able to capitalise on business opportunities."

FFH 2019AR: "On April 18, 2019 Brit acquired the 50.0% equity interest in Ambridge Partners LLC ("Ambridge Partners") that it did not already own for $46.6, remeasured its existing equity interest to fair value for a gain of $10.4, and commenced consolidating Ambridge Partners."

FFH 2016AR: "In 2015 Brit purchased 50% of Ambridge Partners, one of the world's leading managing general agencies of transactional insurance products. In 2016 Ambridge produced gross premiums written of $32 million for Brit at a combined ratio well below 100%."

FFH 2015AR: "In December, Brit made an investment in Ambridge Partners, one of the world's leading managing general underwriters of transactional insurance products. These products insure losses as a result of breaches or inaccuracies in warranties and indemnities relating to M&A, restructuring activities, business financing and tax issues. Ambridge, which has been a partner of Brit for the last nine years, produces $128 million of premiums and is highly profitable. We welcome Jesseman Pryor (CEO), Jeffery Cowhey (President) and their team of 29 employees to Fairfax."

Pet Insurance – June 2022

Aug 1, 2022

With the release of Q2 results we got additional information on the pet insurance sale to JAB. This must be one of the best investments Fairfax has ever made. The after-tax gain is $975 million ($41/share) and will be booked when the sale closes later this year. For a business with $350 million of revenue (if I understood the Q2 conference call correctly).

Fairfax made two purchases in 2013 and 2014. The pet insurance business was cultivated within Fairfax for 10 years. The pandemic likely accelerated the growth of the business. And now Fairfax is opportunistically exiting/selling at what looks to be a premium price. And selling this business looks like it will have little impact on Fairfax's future insurance business (top or bottom line).

We like to obsess over Fairfax's many investment failures over the years. Farmers Edge being the most recent example. The flip side of the coin is Fairfax has many examples of where they have hit the ball out of the park.

Most importantly, the gain from the sale of the pet insurance business will not be used to cover significant realized losses in the investment portfolio (those days are hopefully in the rear-view mirror). Instead, the significant gains will be used to build future shareholder value. This is a significant NEW development for Fairfax. And that prospect should get all Fairfax shareholders very excited.

Fairfax is now, after 7 lean years, finally playing offence again. Strong underwriting + solid investment gains is now driving significant growth in BV per share. 2021 was the start. Much more is coming. Eventually investors will figure it out.

"Fairfax will receive approximately $1.4 billion in the form of approximately $1.15 billion in cash and $250 million in seller promissory notes, and the company will also invest $200 million in JCP V, a JAB consumer fund."

"The transaction is expected to close in the second half of 2022. On closing the transaction the company expects to record an after-tax gain of approximately $975, and deconsolidate assets and liabilities with carrying values at June 30, 2022 of approximately $150 and $32."

A look back: media releases of Fairfax's acquisition of Hartville in 2013 and Pethealth in 2014.

TORONTO, ONTARIO--(Marketwired - May 15, 2013) - Fairfax Financial Holdings Limited (TSX:FFH) announces the signing of a merger agreement with Hartville Group, Inc., of Canton, Ohio, pursuant to which Hartville will become wholly-owned by Crum & Forster's United States Fire Insurance Company. The transaction, which is subject to customary conditions including regulatory approval, is expected to close early in the third quarter of 2013.

Hartville, one of the oldest and largest pet insurance providers in the U.S., provides pet insurance plans under several brand names, including Hartville Pet Insurance and the Petshealth Care Plan. Hartville also is the exclusive strategic partner for pet insurance with The American Society for the Prevention of Cruelty to Animals®.

"We are very excited to have Hartville join the Fairfax group," said Prem Watsa, Chairman and CEO of Fairfax. "This acquisition represents a new phase in our existing relationship with Hartville through Fairmont Specialty. As a result of the vertical integration created by this merger, Hartville's pet insurance programs will be uniquely positioned in the industry to generate sustainable growth."

TORONTO, ONTARIO, August 29, 2014 – Fairfax Financial Holdings Limited (TSX: FFH) and Pethealth Inc. (TSX: PTZ) announced today that they have entered into an arrangement agreement under which Fairfax will acquire all of the outstanding common shares of Pethealth for $2.79 per share in cash. In addition, under the terms of the transaction, Fairfax will acquire all of the outstanding preferred shares of Pethealth for a purchase price of $2.79 per share in cash, plus any dividends accrued but unpaid up to, but excluding, the day of closing.

The purchase price represents a premium of approximately 26% to the closing price of Pethealth's common shares on the TSX on August 29, 2014 and a premium of approximately 69% to the closing price of Pethealth's common shares on the TSX on August 15, 2014. The purchase price also represents a premium of approximately 69% to Pethealth's volume weighted average share price for the twenty trading days ending on August 15, 2014 and a premium of 36% to the all-time high price of Pethealth's common shares prior to such date.

Total cash consideration of approximately $100 million will be paid for Pethealth's common and preferred shares and options. The transaction, which will be completed by way of a plan of arrangement (the "Arrangement"), is subject to certain customary closing conditions, and is expected to close in the fourth quarter of 2014.

Resolute Forest Products – July 2022

March 2023

On March 1, 2023, the sale of Resolute Forest Products to The Paper Excellence Group closed. The deal was announced July 6, 2022. This is GREAT NEWS for Fairfax shareholders on so many fronts. Proceeds to Fairfax from the sale of RFP is $626 million cash plus a $183 million contingent value reserve (CVR – linked to any refund in the future of softwood duties already paid).

RFP was sold at $20.50/share. For perspective, back in March 2020, RFP shares traded at $1.20/share. Fairfax owned 30.5 million shares so RFP's market cap 2 short years ago was a total of $37 million. Pre-pandemic, RFP's shares traded at an average of about $6/share. In the record high lumber market of 2021, RFP's shares traded at an average of about $12/share. Bottom line, at $20.50, Fairfax got an outstanding price for this company.

But price is just the beginning of why this is a great move for Fairfax shareholders. RFP also owns some pretty crappy businesses: newsprint, paper and tissue. And the 'good' business, lumber, is getting killed today by higher interest rates (yes, I do like lumber looking out a year or two). I think RFP also had a large pension liability on its books. Bottom line, Fairfax sold what was overall (still) a challenged business.
There is also the psychological benefit of Fairfax selling RFP. This shouldn't matter - but it does. RFP was one of Fairfax's larger purchases (total investment of $791 million) from a decade ago. It was also one of Fairfax's great investment busts. This train wreck of an investment started all the way back in 2008 when Fairfax spend $350 million on a convertible bond of Abitibi (the predecessor of RFP). And as 'the story' kept getting worse, Fairfax kept buying more. Also buried in RFP's sad history was the smelly (putting it politely) take-out in 2012 of Fibrek (SFK Pulp). I am guessing there are lots of long-term shareholders of Fairfax who are very happy that Fairfax has sold RFP. It is yet another example of 'old Fairfax' being laid to rest by the current team at 'new Fairfax'.

The good news part of the RFP story (other than the price it sold for) is Prem admitted in his letter in the 2018AR (and again in the 2019AR) that RFP had been a very poor investment. Terrible business. Poor management (back in the day). Double down. I think the 'lessons' of RFP was taken to heart by Fairfax back in 2018. And shareholders have been reaping the reward ever since. Fairfax has been making much better decisions on new equity purchases - putting a premium on management among other things.

As of March 1, 2023, in the midst of a bear market in financial assets, Fairfax has $620 million to redeploy into higher quality investments. Given their solid track record over the past 5 years in deploying capital I can't wait to see what Fairfax does.

To be fair, the management team at RFP has done a very good job in recent years. The purchase of the three lumber mills in the US south in 2020 (at the bottom of the lumber cycle) was timed perfectly. Bottom line, they got the company to a position where it was taken out at a good price.

Comments from Prem about Resolute Forest Products from Fairfax's 2022AR.

"In July 2022, Resolute agreed to be purchased by the Paper Excellence Group. The cash portion of the deal, $20.50 per share, represented a 64% premium to Resolute's pre-announcement price. Resolute's shareholders will also receive contingent value rights tied to potential duty deposit refunds of up to $500 million. Fairfax, which held 40% of Resolute, agreed to vote in favour of the deal."

"Paper Excellence's acquisition of Resolute closed on March 1, 2023. Our journey with Resolute began in a significant way in April 2008 with the purchase of approximately $350 million of an 8% AbitibiBowater convertible bond (at $10 per share) – almost 14 years ago! We added to our investment in Resolute in common shares and bonds over the years with a net investment after dividends of $715 million. With the interest income received on our bonds, sale proceeds of $622 million and with a little bit of good fortune on our remaining holdings in the contingent value rights, we may end up breaking even over this long holding period – although clearly a very poor long-term return. A big thank you to Remi Lalonde, Duncan Davies and Brad Martin for leading a strong turnaround in Resolute's results over the last few years." *Prem Watsa – Fairfax 2022AR*

Comments from Prem about Resolute Forest Products from Fairfax's 2018AR.

"We have invested $791 million in Resolute and received a special dividend of $46 million, for a net investment cost of $745 million. Our initial investment was a convertible bond purchased in 2008 for $347 million. We invested an additional $131 million prior to Resolute entering into creditor protection and most of the remainder during the period from December 2010 to 2013. Subsequent to write-downs and our share of profits and losses over time, at December 31, 2018 we held our 30.4 million Resolute shares in our books at $300 million ($9.87 per share). The current fair market value of these shares is $244 million ($8.03 per share). You can see that Resolute has been a very poor investment to date!" *Prem Watsa – Fairfax 2018AR*

For long term shareholders, here is a trip down memory lane for RFP. A link to historical milestones at the company from 2008 to present…

https://www.resolutefp.com/About_Us/Our_History/

A List of Privately Held Asset Sales - 2021

Date: 2021

Fairfax has been 'monetizing' several of their privately held non-insurance holdings over the past couple of years. Fairfax's definition of monetization is broad and includes not just out-right sale (exiting entire holding) but also spinning the holding into the public markets (where they usually retain a controlling interest). Over the past 2 years they have 'monetized' more than $1 billion worth of assets. And they still have private investments worth more than $1 billion (my guess) so they likely are not done in their effort to 'surfacing value'.

This 'monetization' drive has been a stated priority for Fairfax. I would love to hear from other board members on why Fairfax is moving so aggressively in this direction. Are they recognizing Hamblin Watsa is not a turn-around shop? Is it so the value of the individual holding gets reflected more accurately in BV? Is it to position the holding so it can be more successful? The amount of cash going to Fairfax has been pretty minimal, so this does not look like a focus.

One big benefit for shareholders of the 'monetization' process is disclosure. Given the limited disclosure it is very difficult for investors to value the private holdings especially a couple of years after purchase. By reducing the number and size of private holdings Fairfax is making it easier for investors to understand, follow and attach a value to their many remaining equity holdings.

I have included APR and Fairfax Africa in the 'sale' bucket because these assets are no longer managed directly by Fairfax. BIG WIN.
Fairfax has been very opportunistic on the IPO front. The funds raised by these companies will be used to fund future growth/pay down debt. BIG WIN.

Bottom line? Fairfax has strengthened their remaining collection of equity holdings with these moves (taken as a whole). And to have achieved this much during Covid is impressive.
Future moves? Seven Islands IPO still on? Anchorage IPO in 2022? Digit IPO 2022?

<u>Sales</u>: outright sale/significant change in management (Fairfax no longer involved)

1.) APR - sold to Atlas - March 2020 - proceeds of $200 million (18 million Atlas shares at $11.10 per share)
2.) Fairfax Africa merger with Helios - July 2020 - owns 32% of new publicly traded entity
3.) Davos Brands - sold to Diagio - Sept 2020 - proceeds $59 million + consideration of $36 million (depending on brands performance) - cost (2016) was $50
4.) Easton baseball (part of Peak Ach) - sold to Rawlings - Dec 2020 - cash proceeds $65 million plus 28% ownership position in Rawlings (#1 manufacturer in baseball) - gain on sale of $15 million
5.) Rouge Media - sold in Q1 2021 - proceeds of $10 million
6.) Toys 'R Us - sold retail business - Aug 2021 - no financial terms provided - sold to Putnam Investments. Still own the real estate.

IPO's/Mergers/Reverse Takeover: resulting in significant funds being raised to support growth prospects of company.

7.) Dexterra (Carillion) reverse takeover of Horizon North - May 2020 - own 49% of publicly traded entity - carried on balance sheet at $3.62 vs market value of $5.06
8.) Farmers Edge IPO - March 2021 - own 59.9% of publicly traded entity - raised $114 million
9.) Boat Rocker IPO - March 2021 - own 45% of publicly traded entity - raised $136.5 million
10.) Chemplast Sanmar IPO (Fairfax India) - Aug 2021 - subsidiary of Sanmar (Fairfax India has 42.9% equity interest in Sanmar).

Remaining Collection of Private Investments:

1.) Peak Achievement - Bauer Hockey (owned with Sagard Holdings)
2.) AGT - taken private Feb 2019
3.) EXCO - emerged from bankruptcy protection June 2019 - 44% ownership
4.) Mosaic - taken private June 2021
5.) Ant Media
6.) Sporting Life and Golf Town - 61% ownership of each
7.) Rawlings - 28% ownership - Dec 2020 - Seidler Equity Partners are controlling shareholders
8.) Chorus Aviation
9.) Small positions - Praktiker, Kitchen Stuff Plus and William Ashley

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Monetizations - a little more information from old Fairfax annual reports.

1.) APR Energy:

- 2020AR: sold APR Energy to Atlas in exchange for 18 million shares at $11.10 per share

2.) Fairfax Africa/Helios:

- 2020AR: "2020 was another disappointing year for Fairfax Africa with net losses of $207 million. To strengthen the platform, we merged Fairfax Africa and Helios Investment Partners (HIP) to form Helios Fairfax Partners ("HFP"), forming the premier Africa-focused alternative investment manager, under the leadership of Tope Lawani and Babatunde Soyeye, the co-founders and managing partners of HIP, a private equity firm which they founded 15 years ago and which has had great success investing in Africa. Tope and Baba have assumed the roles of Co-Chief Executive Officers and directors of HFP. Fairfax continues to hold 32% of the equity and 53% of the votes of HFP. Together, Fairfax and Helios will be the ultimate controlling party of HFP. Going forward, investors in HFP will benefit from net management fee income, 25% of carry fee income from the past and half of carry fee income going forward from Helios' private equity funds. This flow through structure will bring a regular stream of earnings and cash flow for HFP in addition to appreciation potential of its cash and investments on the balance sheet. We are very excited about the future prospects for HFP in Africa under Tope and Baba's leadership."

3.) Davos Brands:

- 2020AR: "In 2016 we invested $50 million into Davos Brands (a spirit company) for a 36% interest alongside David Sokol. In September 2020 the company was sold to Diageo: our cash proceeds were $59 milllion and we are eligible to receive additional consideration of up to $36 million, contingent on the brand performance over the next ten years. We hope to see these additional proceeds in the future."

4.) Easton baseball: see Peak Achievement 1.) below

5.) Rouge Media:

- 2020AR: "Subsequent to December 31… the company sold substantially all of its interest in Rouge Media for consideration of approximately $10 and expects to record a nominal gain in the first quarter of 2021."

6.) Toys "R" Us:

- 2018AR: Acquisition of Toys "R" Us (Canada) Ltd.: "On May 31, 2018 the company acquired a 100% equity interest in Toys "R" Us (Canada) Ltd. ("Toys "R" Us Canada") from Toys "R" Us – Delaware, Inc. for cash consideration of $41.1 (Cdn$53.3) and an additional investment of $193.7 (Cdn$251.3) that Toys "R" Us Canada used to repay its debtor in possession financing loan. Toys "R" Us Canada is a specialty retailer of toys and baby products with 82 stores across Canada. The assets, liabilities and results of operations of Toys "R" Us Canada were consolidated in the Other reporting segment."

7.) Dexterra:

- 2020AR: "The development of Dexterra's business was dramatically reshaped by the reverse takeover in May 2020 of Horizon North. Dexterra, now a listed public company and led by John MacCuish, has a vision to build a Canadian support services champion. Its activities include a comprehensive range of facilities management, workforce accommodations, and forestry and modular build capabilities, including being a leader in social housing projects. Dexterra has publicly stated that it is on course in the next few years for Cdn$1 billion in revenue and Cdn$100 million in EBITDA."

- 2018AR: "I am happy to report that we also made two significant private company investments in 2018/2019 – Dexterra and AGT. Dexterra, led by John MacCuish as CEO, is the new name for Carillion Canada which went into bankruptcy because of the bankruptcy of its parent in the U.K. Dexterra provides industry-leading facilities management and operation solutions across Canada, including maintenance solutions for over 50 million sq. ft. of high-quality infrastructure. This includes some of the country's largest airports, premier retail and commercial properties, corporate campuses, research and education facilities, large industrial sites, defence and public assets and state-of-the-art healthcare infrastructure. The company is also one of the country's largest reforestation contractors – planting over 40 million trees annually, it annually completes 4,400 hectares of forest thinning/brushing and 1,200 hectares of site preparation–it employs hundreds of firefighters, with an emphasis on Indigenous communities, and for the last 30 years it has been supplying and operating full-service remote workforce services. We were able to buy Dexterra at about 5x free cash flow."

8.) Farmers Edge:

- Q2 2021 Earnings Report: "During March 2021, Farmers Edge completed an initial public offering for Cdn$143.8 ($113.8). Prior to the initial public offering the company exercised its warrants and converted its convertible debentures for common shares of Farmers Edge and another third party converted its convertible debentures for common shares of Farmers Edge, resulting in the company's controlling equity interest in Farmers Edge increasing to 59.9% on completion of the initial public offering and capital transactions."

9.) Boat Rocker:

- Q2 2021 Earnings Report: "On March 24, 2021 Boat Rocker completed an initial public offering for Cdn$170.1 ($135.5). Prior to the initial public offering the company converted its convertible debentures for subordinate voting shares of Boat Rocker, and Boat Rocker converted its preferred shares to subordinate voting shares and issued additional subordinate voting shares to a third party, resulting in the company having an economic and voting interest in Boat Rocker of 45.0% and 56.1% on completion of the initial public offering and capital transactions."

- Q2 2021 Earnings Report: "The initial public offerings and related capital transactions at Farmers Edge and Boat Rocker during the first six months of 2021 described above increased non-controlling interests by $242.6"

10.) Chemplast Sanmar (CSL):

- Fairfax India Aug press release: "Fairfax India currently owns 398,853 equity shares of Sanmar, representing a 42.9% equity interest in Sanmar (on a fully-diluted basis) and, therefore, a 42.9% indirect equity interest in CSL prior to the completion of the IPO. It is anticipated that, following completion of the IPO, Fairfax India (through Sanmar) will own an approximate 23.6% indirect equity interest in CSL based on the terms of the IPO. As at June 30, 2021, Fairfax India had valued its equity interest in Sanmar at $438.5 million. Assuming successful completion of the IPO, and assuming an offering within the price range noted above, the value of Fairfax India's equity interest in Sanmar will remain unchanged. CSL is a leading specialty chemicals manufacturer in India with a focus on specialty paste PVC resin and custom manufacturing of starting materials and intermediates for the pharmaceutical, agro-chemical and fine chemical sectors. CSL also wholly-owns Chemplast Cuddalore Vinyls Limited, the second largest manufacturer of suspension PVC resin in India. Sanmar is the ultimate holding company of CSL."

Remaining collection of Private Investments:

1.) Peak Achievement:

- 2020AR: "Fairfax continues to jointly own Peak Achievement with our partner, Sagard Holdings led by Paul Desmarais III. Peak's core assets are Bauer, the leading hockey brand,

and Easton, the number three manufacturing player in baseball. During 2020 Peak merged Easton with Rawlings, the clear number one manufacturer in baseball. The transaction resulted in $65 million cash paid to Peak, while retaining a 28% stake in Rawlings. Peak is now partnered with Rawlings' controlling shareholder, Seidler Equity Partners. Fairfax recognized a $15 million gain on the sale of Easton which closed just before year end. We are excited about the opportunities at Peak, driven by Ed Kinnaly and his team to focus on the core hockey business."

2.) AGT:

- 2020AR: "Global demand for healthy food fueled by population growth, changing consumer attitudes and rising incomes in emerging markets, particularly Asia, are providing excellent business fundamentals for our investment in AGT, a global food champion. Murad Al-Katib and his team are true innovators in developing and supplying plant-based and staple foods to retail, food service and the consumer products sector in over 100 countries around the world. AGT, acquired in 2019, delivered a strong performance in 2020, including 20% growth and record EBITDA."

- 2019 AR: Privatization of AGT Food and Ingredients Inc. "On April 17, 2019 AGT Food & Ingredients Inc. ("AGT") completed a management-led privatization for Cdn$18.00 per common share. The buying group, comprised of the company, AGT management and other co-investors, acquired through a newly formed subsidiary of the company ("Purchase Co.") all AGT common shares not already owned by the buying group for cash consideration of $226.5 (Cdn$301.8), resulting in the company acquiring a 69.9% controlling equity interest in AGT upon closing and effectively settling the company's pre-existing interests in AGT's preferred shares and warrants at fair value."

- "Contemporaneously with the acquisition of AGT, Purchase Co. acquired the company's preferred shares and the remaining common shares of AGT held by the buying group in exchange for its own common shares which diluted the company's interest in AGT to 59.6%, with AGT management and other co-investors owning the remainder. Purchase Co. and AGT subsequently amalgamated and the amalgamated entity was renamed AGT. The company holds warrants that, if exercised, would increase its equity interest in AGT to approximately 80%. The preferred shares were subsequently canceled and the warrants are eliminated on consolidation of AGT. The assets, liabilities and results of operations of AGT were consolidated in the Non-insurance companies reporting segment. AGT is a supplier of pulses, staple foods and food ingredients."

- 2018AR: "AGT, led by Murad Al-Katib as CEO and Hüseyin Arslan as Executive Chairman, is one of the largest suppliers of pulses in the world. With over 2,000 employees, AGT exports pulses (mainly lentils, peas and beans) to over 120 countries around the world. We are helping Murad and Hüseyin take the company private at Cdn$18 per share. The shareholders of AGT have recently approved the deal. We are very excited to be partners with Murad and Hüseyin and expect them to build a very significant company in the global agricultural sector over the long term."

3.) Exco:

- 2020AR: "Fairfax owns 44% of Exco, a U.S. oil and gas producer. Despite weak energy prices in 2020, Exco generated $128 million in EBITDA and $36 million in free cash flow. Net debt fell to $145 million (1.1 times EBITDA). Led by Chairman John Wilder and CEO Hal Hickey, Exco achieved these results through high field level productivity and company-wide cost control. In December, Exco recorded its 73rd month without a lost time incident. Exco's Chairman, John Wilder, is a great partner. We are well served by his leadership."

- 2019AR: "On June 28, 2019 EXCO emerged from bankruptcy protection and settled the company's holdings of EXCO bonds with common shares (note 6), resulting in the company recording a net loss on investment of $179.3 (realized losses of $296.3, of which $117.0 was recorded as unrealized losses in prior years)."

4.) Mosaic Capital:

- Q2 2021 Earnings Report: "On June 25, 2021 Mosaic Capital entered into a privatization arrangement with a third party purchaser pursuant to which the company will exchange its current holdings of Mosaic Capital debentures and warrants, and cash of approximately $11 (Cdn$13.3), for approximately $132 (Cdn$163.3) of newly issued Mosaic Capital 25-year debentures. The company will also acquire a 20.0% interest in the purchaser for approximately $4 (Cdn$5.0). Closing of the transaction is subject to regulatory and shareholder approvals and is expected to occur in the third quarter of 2021. Accordingly, all of the assets and liabilities of Mosaic Capital were presented in assets held for sale and liabilities associated with assets held for sale on the company's consolidated balance sheet at June 30, 2021."

- 2020AR: "In 2017 Fairfax invested Cdn$100 million in preferred shares yielding 6% per annum, Cdn$50 million in senior secured debentures yielding 5% per annum and 17 million warrants of Mosaic, implying a fully diluted ownership of 61%. Chairman John Mackay and CEO Mark Gardhouse have done an outstanding job building a portfolio of established businesses in niche markets across western Canada and Ontario. Since our investment, Mosaic has generated approximately Cdn$70 million in free cash flow and in the very difficult 2020 year managed its western Canada businesses well."

5.) Golf Town & Sporting Life:

- 2020AR: "Fairfax has invested Cdn$74 million for its current 71% stake in the combined business of Golf Town and Sporting Life. Chad McKinnon and his team had an outstanding year. They manoeuvred through COVID-19 lockdowns and maximized results at Golf Town when the stores reopened while also making steady progress in re-aligning the Sporting Life franchise. Both Golf Town and Sporting Life have counter-seasonal aspects which help with working capital management and the combination of the two businesses has resulted in meaningful cost synergies."

6.) Rawlings: see Peak Achievement 1.) above

Chapter 14: Top 10 Lists

Beginning in 2019, at the end of each year I have put together a 'Top 10' list of the most important events that happened at Fairfax during the year (good and bad). The lists when read together provide an interesting five-year chronological perspective of Fairfax as a company. It is amazing all that the company has been able to accomplish over this short time period.

Please note, these posts were made in late December or early January, so they do not include items that were communicated when year-end results were released in mid-February.

2019 Top 10 List: The Supertanker is Turning

Dec 28, 2019

Fairfax has had a very active 2019. For fun, I decided to try and come up with a 2019 'Top 10' list of events driving value for shareholders. Some events were driven by Fairfax (corporate/subsidiaries) and some were driven by management teams in the stock/equities held. On balance, it is clear to me that Fairfax has done many things to build a more valuable company for shareholders over the past year. As a result, the Fairfax 'super tanker' is slowly turning to the benefit of shareholders.

Here is a summary of the types of items impacting shareholder value:

- Being positioned to capitalize on hard market at insurance subs
- Solid growth in interest and dividend income
- Seeding new/newer investments: Seaspan (tranche 2)
- Monetizing mature investments: sales of ICICI Lombard and 40% of Riverstone UK.
- Merging investments to make the whole stronger: Eurobank/Grivalia
- Selling investment to put it in a better position to thrive: APR Energy
- Simplifying corporate structure to better enable companies to succeed: demerger of Thomas Cook and Quess and split of IIFL into three: Finance, Securities and Wealth

1.) <u>Ongoing</u>: emergence of hard market for pricing in insurance: leading to double digit growth in net premiums written at many of the subs. Looks like double digit growth should continue in 2020.

2.) <u>Ongoing</u>: Solid increase in interest and dividend income: while short of Fairfax's goal of $1 billion, looks to be close to $900 million for 2019, versus $784 in 2018 and $559 in 2017.

- January: Seaspan: tranche 2 of $250m debt at 5.5% = $14m in interest income/year

3.) January - Seaspan: Fairfax's additional $250 million investment = 37 million shares purchased at cost of $6.75; with shares currently trading at $14.25 paper gain = $278 million.

- 25 million additional warrants exercisable at $8.10 = paper gain of $154 million

4.) Eurobank: stock closed at €0.54 on Dec 31, 2018. Today the stock is at €0.92; paper gain = US $400 million. Eurobank looks well positioned.

- April: merger with Grivalia improved balance sheet
- April: Cairo Securitization - plan to hive off €7.5 billion chunk of underperforming assets is now almost complete (target Q1 2020).
- July: election of pro-business government in Greece with clear majority in parliament. Lowered corporate tax rate.

5.) Sept/Oct: ICICI Lombard sales: of remaining 10% position for proceeds of US $729 million; recorded a net gain on investments of $240 million in 2019 (there was more in previous years).

6.) December: OMERS paid US$560 million for 40% of Riverstone UK, which gives it a total value of $1.4 billion. Will increase BV by $10/share.

7.) Fairfax India: book value is up significantly in 2019 (+$3/share). BIAL looks like a jewel of an investment that will grow double digits for years to come.

- Dec 16 - Bangalore International Airport (BIAL): Fairfax India to sell an 11.5% interest in Anchorage Infrastructure (holds airport investments) for gross proceeds of 9.5 billion Indian rupees ($134-million). Fairfax India's ownership of BIAL will fall from 54% to 49%. As a result of the transaction, Fairfax India will record investment gains of approximately $506 million, an increase in book value per share of $3.30 per share. The investment gains are supported by positive operational developments at BIAL. For the 12-month period ending October 2019, total traffic at BIAL was approximately 33.7 million passengers. The second runway commenced operations in December 2019. The expansion project for a second terminal at BIAL is expected to be completed in 2021.

- Dec 23 - Sanmar Chemicals Group: completed its announced transaction with Fairfax India. During the period since announcing the transaction in the third quarter of 2018 through September 30, 2019, Fairfax India recorded investment gains from the Sanmar common shares and bonds of approximately $210 million and $100 million, respectively.

8.) November: Sale of APR Energy to Seaspan: moved an underperforming unit into a better situation; obtained Seaspan shares is return.

- APR Energy: US $300 mill / $11.10 per share = 27m shares of Seaspan
- $14 (share price today) - $11.10 (cost) = $2.90 x 27m shares = $78 million paper gain

Under-performers:

9.) Recipe. Shares fell from CAN $26.19 to about $19.50 = $180 million paper loss. Hard to see this turning around any time soon. Restaurant stocks in Canada have been crushed this year. Most provinces are increasing minimum wages aggressively and will be doing so in the coming years as well, which is a negative for the hospitality industry. The good news is the assets are quality and have value; at $19.50 they look cheap.

10.) Blackberry: shares fell from US $11.17 to about $6.50 = $220 million paper loss (double if you include convertible shares they own). The purchase of Cylance has not resulted in the growth expected. Most recent quarter results were ok. If they can get the Cylance unit growing the shares should do well. 2020 will be very interesting to watch.

11.) Resolute Forest Products: shares fell from US $7.93 to about $4 = $120 million paper loss. In December purchased 3 sawmills in US South for $150 million; should new home construction in US pick up in 2020 this could become a solid acquisition for RFP.

Not sure what to think.

12.) AGT take-private

More work needed (by me to understand the businesses):

13.) Indian Investment: Quess, Thomas Cook, IIFL Finance - Securities – Wealth

- there was a lot of noise with these investments in 2019. Thomas Cook demerged its Quess stake and IIFL split into three. This made it difficult to follow. The good news is these five firms are now independent with easy-to-understand share structures; we know how much Fairfax owns of each. And it will be much easier to monitor and understand what is happening moving forward.

Quess: Amazon investment suggests Quess is undervalued. Quess also looks like another jewel of an investment set to grow at double digits for many years to come.

- July - Amazon invested US$ 7.43 million for a 0.51% stake in Quess ($ went to fund growth of Qdigit unit); they paid INR 676/share and market price at the time was INR 430 (they paid a 50% premium).
- December: Thomas Cook India demerged their 50% holding in Quess Corp in order to simplify the corporate structure.

Missing from my original list:

Digit Insurance: a start-up. Fastest growing general insurer in India

- https://timesofindia.indiatimes.com/business/india-business/pes-value-insurance-tech-startup-digit-over-800m/articleshow/72448746.cms

2020 Top 10 List: Holding Pattern (Global Pandemic)

Dec 28, 2020

Fairfax has had a very eventful 2020. Below is a Top 15 list of events driving value for shareholders this year. I would characterize 2020 as a 'holding pattern' kind of year given all the disruption caused by covid and its impact on Fairfax, insurance subs and equity investments. Looking at both 2019 and 2020 there is lots going on under the hood at Fairfax.

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FFH stock price:	Dec 31, 2019 = US $469	Dec 28, 2020 = $336	-28%
BV:	Dec 31, 2019 = US $486	Sept 30, 2020 = $442	
Dividend:	$10 (Jan 2020).		

1.) Covid

- hit to BV of $54/share in Q1 - primarily due to unrealized losses in investment portfolio (lots of cyclical companies)
- resulted in losses at insurance subs, led by Brit, of $535.6 million through Q3

2.) Insurance - hard market confirmed

- net premiums written up 12.7% in Q3, 2020
- expected to continue strong growth in 2021

3.) Sale of Riverstone UK

- sale providing much needed cash in 2 transactions.
- 40% sold - closed March 31; proceeds of US$599.5
- remaining 60% - to CVC Strategic Opportunities Fund II (will close early 2021) for approximately US$750 million at closing + up to US$235.7 million post-closing under a contingent value instrument.
- https://www.globenewswire.com/news-release/2020/12/02/2138249/0/en/Fairfax-Announces-Sale-of-RiverStone-Europe-to-CVC.html

4.) Common Stock and Equity Index Short Positions

- Q3 net realized loss = $168 million
- First 9 months realized loss = $391 million
- Biggest negative for the year (under Fairfax control)

5.) Increase in total debt

- April 24: additional $650 million at 4.625%

6.) Fixing Mistakes

- APR sale to Atlas closed Feb 2020 - Atlas issued approximately 29.9 million ATCO shares to APR sellers as equity consideration, at a deemed value of $11.10 per share.
- Fairfax Africa / Helios - Helios will acquire a 45.9% voting and equity interest in Fairfax Africa in exchange for contributing its entitlement to cash flows from certain fee streams and being appointed sole investment advisor to Fairfax Africa. Fairfax recorded a non-cash net loss on investments of $164 million in consolidated statement of earnings.

7.) Opportunistic Bond Purchases during pandemic

- from Q1 report: US corporate bonds of $2.9 billion; avg maturity of 4 years; int rate of 4.25%; avg maturity of 4 years; interest income of $123 million per year

8.) Blackberry - new convertible debentures – September

- Fairfax redeemed $500 million 3.75%
- Fairfax subscribed $330 million 1.75%; $6 conversion (55 million shares)

9.) Digit (India) continues strong growth (30% versus flat for overall insurance market) and expects to reach break-even by end of year

- https://m.dailyhunt.in/news/india/english/money+control+english-epaper-mconten/insurance+startup+digit+set+to+break+even+by+the+end+of+this+year-newsid-n231552142

10.) Buying out minority partners

- Brit - 9.4% - Aug for $220 million - now owned 100% by Fairfax

11.) Positioning Non-Insurance Companies to Succeed

- Dexterra - reverse acquisition of Horizon North Logistics - closed in March https://www.newswire.ca/news-releases/horizon-north-and-dexterra-sign-definitive-agreement-to-create-leading-canadian-support-services-company-898386935.html
- Easton Baseball sold to Rawlings (Seidler Equity Partners) - Existing shareholders of Peak Achievement Athletics Inc., the parent of Easton, will continue to participate as minority owners in the combined organization. https://www.prnewswire.com/news-releases/rawlings-enters-into-definitive-agreement-to-acquire-easton-diamond-sports-301156058.html

12.) Monetizations

- Davos Brands - Sept 30 - for cash proceeds of $58.6 and recorded a net realized gain of $19.3
- Vault insurance - announced Nov - close Q1, 2021 - Allied World sells controlling position; retains 10% ownership https://www.insurancejournal.com/news/national/2020/11/18/591092.htm

13.) Seeding New Insurance Ventures

- Ki Insurance (Brit) - announced in May 2020; open for business Jan 1, 2021. Ki will aim to significantly reduce the amount of time taken for brokers to place their follow capacity. Ki's algorithm, developed with support from University College London, will evaluate Lloyd's policies and automatically quote for business through an always available digital platform, built by Google Cloud and accessed directly by brokers. Ki has raised US$500m of committed capital from two backers: Blackstone and Fairfax. https://www.britinsurance.com/news/ki-platform-goes-live-with-partner-brokers

14.) Insider Stock Purchases

- Prem: $149 million in June at $310/share. https://www.fairfax.ca/news/press-releases/press-release-details/2020/Prem-Watsa-Acquires-Additional-Shares-of-Fairfax/default.aspx
- Others at Fairfax also were buying.

15.) Stelco (Fairfax owns 13 million shares; cost CAN$20.27)

- Amazing year; stock price: Jan 1 was CAN$10.91. In March the stock went to $3.24 per share. Dec 28 the stock closed at $22.11 per share.
- Most importantly the company is positioned very well looking ahead to 2021 and what looks like a bull market for steel pricing; investment phase in the business is ending and Stelco is focussed on maximizing free cash flow generation and rewarding shareholders.

Personnel Changes

- Feb: Paul Rivett (President of Fairfax) retires
- Nov: Scott Carmilani (former CEO of Allied) resigns to run Vault
- APR: Q2 former CEO of APR left (under Atlas umbrella). June Brian Rich appointed as new President and COO.

2021 Top 10 List: Emergence of 'New Fairfax'

Jan 31, 2022

Fairfax has had an outstanding 2021. In fact, it was one of the best years in Fairfax's history. Below is a Top 10 list of what drove value for shareholders of Fairfax in 2021.

I would characterize 2021 as the year the 'new Fairfax' finally started emerging for all to see. Fairfax had been making important changes under the hood for the past 4-5 years and 2021 was the year all the hard work finally started to be reflected in the reported financial results.

FFH stock price increased 45% in 2021

- Dec 31, 2021 = $492.13 Dec 31, 2020 = US$340

BV increased 18% in the 9 months to Sept 30 (BV will be higher when Q4 is reported)

- Sept 30, 2021 = US$561.88 Dec 31, 2020 = US$478.33;

Dividend of US$10 dividend was paid Jan 2021

2021 Top 10 List

1.) Net gains on investments of $2.5 billion (to Sept 30) = $96/share

- Equities + Digit revaluation + FFH TRS
- does NOT include pending gain on Digit of $1.1 billion (Digit should be on its own but I decided to include it here).
- FFH TRS: 1.96 million shares at cost of US$396/share. Classic Fairfax move: creative, unconventional, opportunistic, smart, well timed, profitable

2.) Increase in fair value of investments in associates of US$1,372 million (to Sept 30) = $53/share

- this gain is in addition to 'gains on investments' summarized above.
- this gain is NOT captured in BV.

3.) Significant increase in net premiums written of US$2.3 billion (to Sept 30) = growth of 20.5%

- hard market that began in Q4 2019 is continuing as we begin 2022

4.) US$1 billion share buy-back Dec: 2 million shares purchased (7% of shares outstanding) at US$500/share

- financed through sale of 10% interest in Odyssey for US$900 million
- share buybacks done below intrinsic value are very accretive for long term shareholders.
- second classic Fairfax move of 2021: creative, opportunistic, smart, well timed

5.) Debt reduction: total debt was paid down. Combined with significant earnings in 2021, debt ratios have improved considerably.

- largely paid with proceeds from sale of the remainder of Riverstone for US$700 million and 14% interest in Brit for US$375 million.

6.) Underwriting profit increased $182 million (to Sept 30)

- YTD Sept 30, 2021 = $330; YTD Sept 30, 2020 = $142 million
- given hard market we should see continued improvement in underwriting profit in 2022 (as written premiums become earned)

7.) Fairfax's two largest equity holdings look well positioned as we begin 2022 and the shares are very cheap:

- Atlas: executed and completed financing on very aggressive new build strategy in 2021. We could see 15-20% EPS growth each year for the next 3 years.
- Eurobank: completed multi-year fix of balance sheet in 2021 and is now poised to grow business and earnings and leverage improving Greek economy

8.) Gulf Insurance Group: completed acquisition of AXA Gulf, increasing in size by about 80%

9.) A number of Fairfax equity holdings completed significant stock buy backs in 2021, significantly increasing Fairfax's ownership percent: Fairfax India, Stelco, Resolute Forest Products

10.) Changes at private holdings:

- Eurolife stake was increased to 80%
- Pethealth was folded into Crum (Jan 1, 2021)
- Toy 'R Us retail operations were sold (kept real estate)
- Boat Rocker IPO - raised C$170 million - very opportunistic
- Farmers Edge IPO - raised C$125 million -very opportunistic (even though the business continues to struggle)

The bad

1.) Drop in interest and dividend income of $109 million (to Sept 30)

- Sept 30 2021 = $496 million from Sept 30, 2020 = $605 million
- decline is due to Fairfax reducing duration on bond portfolio
- this strategy (low duration) carries a short-term cost
- however, should bond yields move higher (as is currently happening as we begin 2022) Fairfax is well positioned to benefit

2.) Continued losses from what is left of runoff; what will average loss be moving forward? -$25 million/quarter?

2022 Top 10 List: Operating Income Spikes

Fairfax has had an outstanding 2022. I characterized 2021 as the year the 'new Fairfax' finally started emerging for all to see. We got more of the same in 2022. Fairfax has been making important changes under the hood for the past 4-5 years and 2021 and 2022 are the years in which much of the hard work is being more fully reflected in the reported financial results. Most importantly, operating income (underwriting profit + interest and dividends + share of profit of associates) is spiking higher.

<u>FFH stock price increased 20% in 2022</u> (to Dec 29)

- Dec 29, 2022 = US$591.73 Dec 31, 2021 = $492.13

S&P500 is down 19% so Fairfax's outperformance of close to 40% has been significant in 2022.

<u>BV decreased 9.5% in the 9 months to Sept 30</u> (BV will likely be much higher when Q4 is reported).

- Sept 30, 2022 BV = US$569.97 Dec 31, 2021 BV = US$630.60

<u>Dividend</u> of US$10 dividend will likely be paid Jan 2022 (it is usually announced in early January).

How can I say Fairfax had a great year in 2022 if BV is down 9.5% Sept YTD? The hit to BV is coming primarily from the spike in bond yields. We just had the worst year for bonds in something like 200 years! To Sept 30, 2022, net losses on investments was $2.3 billion (about $100/share) = $1.4 billion in bonds + $500 million in stocks + $400 million in currency. <u>Counter intuitively, the spike in bond yields is actually the best thing that could have happened to Fairfax in 2022</u>.

Importantly for Fairfax, most of the 'losses' in the bond portfolio will likely reverse over the next year or two as bonds are held to maturity. And moving forward, Fairfax will be generating record amounts of interest income…. see below for the details. I also expect Fairfax to earn +$60/ share in Q4, which if it happens, will push BV for the full year into positive territory. So even though BV will finish 2022 up only slightly, as we will learn below, the future earnings power of Fairfax has never looked better.

<u>2022 Top 10 List</u>

1.) <u>increase in interest income:</u>

- Interest income should increase to a record $830 million in 2022 from $568 million in 2021 which equals an increase of about US$260 million (+45%). In 2023 my guess is interest income will increase further to a staggering $1.37 billion, a $540 million increase (+65%) over 2022, and a 140% increase over 2021. For reference, $1.37 billion = $58/share and FFH shares are trading today under US$600. Fairfax is trading today at about 10X interest income (pre-tax). Nuts. The significant increase in interest income will be the gift to Fairfax shareholders that will keep on giving for years into the future.

- Fairfax has an investment portfolio of about $51 billion. Of this total, about $36 billion is fixed income. Over 2021 Fairfax reduced the duration of their fixed income portfolio to 1.2 years. Most P/C insurers have an average duration closer to 4 years. With such a low duration portfolio, Fairfax has been able to benefit from spiking interest rates by rolling over most of their fixed income portfolio into much higher rates. In Q3 they also started extending the average duration of their fixed income portfolio to 1.6 years by buying longer dated US treasuries (with 3-5 year duration). Increasing duration will lock in high yields for years into the future.

2.) <u>increase in underwriting income:</u>

- Net premiums written will increase to a record $22 billion in 2022 from $17.8 billion in 2021 (+20% growth) and $14.7 billion in 2020 (+50% growth over the last 2 years). In turn, this is spiking underwriting profit which I estimate will come in at a record $970 million in 2022 (95CR est), compared to $801 million in 2021 (95CR) and $308 million in 2020 (97.8CR). In 2023 my guess is net premiums written will increase 15% to $25.4 billion and underwriting profit will increase to $1.1 billion (assuming a 95CR). For reference, $1.1 billion = $47/share. The significant increase in net premiums and underwriting profit will be the gift to Fairfax shareholders that will keep on giving for years into the future.

- What is driving the substantial increase in net premiums written? We are in a hard market for P/C insurance. It started in 2019 and looks like it will continue well into 2023. Re-insurance rates are set to spike higher in 2023 and this should benefit Fairfax as they have a large re-insurance business.

3.) increase in share of profit of associates:

- This source of earnings had a break-out year in 2022. I estimate share of profit of associates will finish 2022 at a record of around $1 billion = $43/share. Over the 5-year period, from 2017-2021, 'share of profit of associates' averaged about $200 million per year for Fairfax. My guess is 'share of profits of associates' could deliver around $1 billion again in 2023.

- That is a huge increase in a very short period. What happened? Put simply, the earnings power of the equity holdings captured in the 'associates-equity accounted' bucket is beginning to shine through. The turnarounds have (finally) turned around (Eurobank). The fast growers are executing well (like Atlas). The commodity bull is running (Resolute, Stelco, EXCO Resources).

4.) significant asset monetization:

- Fairfax pulled a rabbit out of its hat in 2022. On October 31, 2022, Fairfax closed on the sale of C&F Pet Insurance Group and Pethealth to Independence Pet Group (majority owned by JAB Holding Company) for proceeds of $1.4 billion in the form of $1.15 billion in cash and $250 million in seller debentures. In Q4 Fairfax expects to record a pre-tax gain of approximately $1,278 million and an after-tax gain of approximately $992 million ($42/share).

- Bottom line, Fairfax sold a business no one knew they owned for $992 million after tax ($42/share). For a little background, Fairfax purchased Hartville Group for $34 million in 2013 and Pet Health for $89 million in 2014 and in 2022 sold the combined entity for $1.4 billion. That is nuts. Fairfax has a long history of buying small insurance businesses and patiently growing them over a decade or more and then selling them for very large gains: First Capital, ICICI Lombard, Riverstone UK and now C&F pet insurance. Very impressive. Makes one wonder what else Fairfax has in the cupboard that is under-appreciated by investors?

5.) asset monetization:

- Sale of Resolute Forest Products to Domtar for cash of $626 million + $183 million contingent value right (tied to duties collected). The timing of this sale was perfect. Resolute was sold at a high price ($20.50/share). When it closes proceeds can be rolled into other investment opportunities at bear market lows. Regulatory approval for the deal was just given (late Dec). As much as I like the lumber part of the business over the next 5 years or so... the newsprint/paper part of the business looks ugly. Very happy with this transaction.

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With (likely) record underwriting profit and interest and dividend income and significant asset sales, Fairfax generated a significant amount of cash in 2022. We should see more of the same in 2023. This is a significant development for Fairfax. Cash is a very good thing, especially when you are in a bear market and both bonds and equities are on sale (that buy low thing).

So, what did we see Fairfax do with all that cash in 2022? <u>Record equity investments of around $2 billion</u>. Surprised?

6.) <u>take private of 2 businesses</u>:

- Fairfax spent $537 million as follows:
    - July - Grivalia Hospitality ($195 million)
    - August - Recipe ($342 million).
- These are two businesses Fairfax understands very well as they had already owned significant stakes in both for years. Both purchases were highly opportunistic given they were made as we were just emerging from Covid, and the price paid likely reflected depressed earnings (at least in the case of Recipe).

7.) <u>increase ownership stakes in businesses already owned:</u>

- Fairfax spent $506 million as follows:
    - February - Fairfax India ($65 million)
    - March - exercise of Atlas warrants ($201 million)
    - April - exercise of Altius warrants ($78 million)
    - April - Ensign Energy debenture conversion ($9)
    - June - John Keels debentures ($75 million)
    - Oct - exercise Foran Mining warrants ($25 million)

- Dec - Mytilineos ($53 million).

8.) <u>increase partnership:</u>

- Fairfax spent $300 million on preferred equity in Kennedy Wilson. Fairfax has a long history with Kennedy Wilson, going back to 2010. Kennedy Wilson has been Fairfax's real estate partner for over a decade.

When you put 6.) + 7.) + 8.) together… Fairfax spent $1.343 billion, a significant chunk of money, increasing its ownership in businesses that it was already invested in. These are businesses and management teams that Fairfax understands well.

9.) <u>US large cap purchases</u>:

- Over the first 9 months of 2022, Fairfax spent about $350 million:
  - Micron Technologies ($152 million)
  - Bank of America ($96 million)
  - Occidental Petroleum ($54 million)
  - Chevron ($45 million)

- Of interest, coming out of the Great Financial Crisis in 2008-09, Fairfax spent over $1 billion on a bunch of large cap US stocks: Wells Fargo, J&J, US Bancorp, and USG. It would not surprise me to see Fairfax continue to build out their holdings of large cap US stocks in Q4 and into 2023.

10.) <u>increase private equity holdings/partnerships:</u>

- As part of the pet insurance sale, Fairfax invested $450 million in two separate deals with JAB Holdings. JAB is a privately held German conglomerate. The two transactions:
  - $250 million in debentures
  - $200 million in JAB - JCP V investment funds.

- Fairfax already had significant investments/partnerships with other private equity shops like BDT Capital Partners and ShawKwei. The investment in JAB expands and diversifies Fairfax's significant portfolio of private equity type holdings.

When you put 6.) + 7.) + 8.) + 9.) + 10.) together… Fairfax spent around $2 billion on a collection of businesses that look like solid additions to Fairfax's existing portfolio of equity holdings. <u>Nothing flashy. Boring. Low risk. Good value / opportunistic purchases. Sold upside. Just what many Fairfax shareholders have been asking for…</u>

Fairfax is once again planting lots of seeds. Over time, these investments will all grow and compound in value to the benefit of Fairfax shareholders. A larger equity portfolio will drive higher future earnings. And this will drive the stock price higher. This is just another of many catalysts in place at Fairfax. Fairfax is once again playing offence with its investment portfolio.

11.) continue to take out minority shareholders of insurance businesses:

- On Sept 27, 2022, Fairfax increased its ownership interest in Allied World to 82.9% from 70.9% for total consideration of $733.5 million ($228 million hit to retained earnings) funded via $750 million debt offering. Fairfax buying out minority partners is a solid use of cash. Low risk. Solid return.

12.) Fred VanVleet - bet on yourself update:

- FFH total return swap (TRS) investment continues to perform exceptionally well, up $200 million in 2022.
  - FFH share price Dec 30, 2022 = $594/share.
  - FFH share price Dec 31, 2021 = $492/share.
  - TRS = 1.96 million FFH shares. ($594 x 1.96 = $1.164 billion market value.).
- Given Fairfax shares remain crazy cheap, my guess is Fairfax continues to hold this position.

13.) share buybacks:

- To Sept 30, 2022, Fairfax had repurchased 419,000 shares = 1.8%. Common stock effectively outstanding was 23.445 million at Sept 30,2022 and 23.865 million on Dec 31, 2021. My guess is Fairfax continued to buy back shares in Q4, especially after the pet insurance deal closed the end of October. It will be interesting to see how aggressive Fairfax gets with share buybacks in 2023.

14.) share buybacks at Fairfax's equity holdings:

- Both Fairfax India and Stelco bought back shares in 2022 and this boosted Fairfax's ownership stake in each company.

- Fairfax owns/controls 58.4 million shares of Fairfax India (as of Feb 2022). Total share count at Fairfax India has fallen:
  - Dec 31, 2020 = 149.4 million
  - Dec 31, 2021 = 142.2 million
  - Sept 30, 2022 = 138.7 million.
- Fairfax's ownership at Fairfax India increased from 37.3% to 42.1%.

- Fairfax owns 13 million shares of Stelco. Total share count at Stelco has fallen significantly:
  - Dec 31, 2020 = 88.7 million
  - Dec 31, 2021 = 77.3 million
  - Nov 1, 2022 = 55.1 million.
- Fairfax's ownership at Stelco increased in 2022 from 16.8% to 23.6% (significant).

15.) Proposed privatization of Atlas:

- A group (lead by David Sokol) has proposed to take Atlas private at $15.50/share. Fairfax (with 45% stake) is supportive of the deal. Fairfax is not obligated to purchase any additional shares. The deal is expected to close in 1H 2023. This is a massive deal and involves Fairfax's largest equity holdings. I don't have a strong opinion on the proposed deal right now. All things being equal, I think being a private company is better for Atlas. However, I do not like the lack of financial details available on Fairfax's private holdings.

Negatives

1.) increase in net debt of $1.3 billion:

- Net debt Sept 30, 2022 = $7.6 billion.
- Net debt Dec 31, 2021 = $6.3 billion.
- The pet insurance sale closed the end of October so the net debt number will come down when Q4 is reported. It will be interesting to see if Fairfax decides to bump the minimum $1 billion cash at hold co to a higher number moving forward.

2.) impairment charge:

- Non-cash impairment charge on goodwill of Farmers Edge of $109.2 recognized in the second quarter of 2022. Like all large companies, Fairfax has a few warts.

3.) continued losses from what is left of runoff:

- What will average loss be moving forward? -$25 million/quarter?

Personnel Changes

- Feb: Peter Clarke promoted to President of Fairfax

2023 Top 10 List: Fairfax Achieves 'Escape Velocity'

January 9, 2024

At the end of each year, I put together list of what I think are the 10 most important events that have happened at Fairfax during the year (usually in terms of driving shareholder value). This is the fifth year of me doing this list. Reading each of the summaries in succession provides an interesting 5-year view of what has been going on at Fairfax.

'Escape velocity' Fairfax edition, featuring David Bowie - Space Oddity

https://youtu.be/iYYRH4apXDo?si=d4s1WQjQEBdQufBP

Prem to Fairfax investors: "Take your protein pills and put your helmet on."

Fairfax's business and financial results have been steadily improving each of the past three years. 2023 was the year overall company performance achieved 'escape velocity' - finally breaking free from the gravitational pull/orbit of its recent past (2010-2020). The company - its business results/earnings and reputation - is now charting new territory.

Investors have noticed. Fairfax's stock increased 55% in 2023. Over the past 3 years, Fairfax's stock is up 170% and it has outperformed the S&P500 by a staggering 143%.

Fairfax (US$)	Stock Price	YOY change	increase over past 36 months	S&P500	YOY change	increase over past 36 months
Dec 31, 2020	$340.94			3,756		
Dec 31, 2021	$492.13	44%		4,766	27%	
Dec 31, 2022	$594.12	21%		3,840	-19%	
Dec 31, 2023	$920.76	55%	170%	4,770	24%	27%

Book value per share increased at Fairfax by 33% in the 9 months to Sept 30, 2023, and 83% over the past 33 months. My guess is BV will be up nicely in Q4. This is best-in-class performance compared to other P/C insurance peers. The performance of a few that I follow - Chubb, WR Berkley and Markel (all good P/C insurers) - has not come close to the performance of Fairfax over the past three years (in terms of growth of BV/share).

Fairfax	Book Value US$	Book Value Increase	increase over past 33 months
Dec 31, 2020	$478.00		
Dec 31, 2021	$631.00	32%	
Dec 31, 2022	$658.00	4%	
Sept 30, 2023	$877.00	33%	83%

A dividend of US$10/share was paid Jan 2023. Fairfax recently announced the dividend to be paid in January 2024 will increase to $15/share, which is an increase of 50%.

Top 10 'events' driving shareholder value in 2023

1.) Exceptional overall company performance. This might sound like a cop-out. But I don't think so. ALL three of Fairfax's economic engines performed at a very high level in 2023:

- Insurance
- Investments - fixed income
- Investments - equities/derivatives

As a result, Fairfax is poised to deliver - for the second year in a row - record results in each of underwriting profit, interest and dividend income and share of profit of associates. In 2023, operating income per share is poised to increase 43% (to $190/share) over 2022. Over the past three years, operating income per share is up a staggering 415% - this very important measure of company results has indeed achieved 'escape velocity.'

Fairfax - Operating Income				
December 31, 2023	**2020**	**2021**	**2022**	**2023E**
Underwriting profit - ins & reins.	$309	$801	$1,105	$1,373
Interest & dividends	$769	$641	$962	$1,929
Share of profit of associates	-$113	$402	$1,015	$1,100
Operating income - ins & reins	**$965**	**$1,844**	**$3,082**	**$4,402**
Per share	$37	$77	$132	$190
Shares Outstanding Dec 31	26.2	23.9	23.3	23.2

My latest estimate has Fairfax delivering an ROE of about 20% in 2023. That is exceptional performance. But more important than the results delivered in 2023, Fairfax's insurance and investment holdings continue to grow in size and improve in quality. This sets the table nicely for continued earnings growth (and high ROE's) in the coming years.

2.) Extending the average duration of the fixed income portfolio from 1.6 years at Dec 31, 2022 to 3.1 years in October 2023.

Prem Watsa - Fairfax Q3, 2023 Conference Call:
"Recently, in October, during the spike in treasury yields, we have extended our duration to 3.1 years with an average maturity of approximately 4 years, and yield of 4.9%."

Over the past three years, the fixed income team at Fairfax has superbly navigated the company (and Fairfax shareholders) through the greatest fixed income bubble top and subsequent bear market in history. They protected the balance sheet from booking billions in losses. And, by meaningfully extending the average duration, they have locked in high interest income for years in the future.

Fairfax Fixed Income	Average Duration Years	5 year US Treasury
December 31, 2021	1.2	1.26%
December 31, 2022	1.6	3.99%
October 2023	3.1	4.95%

3.) Insurance sub Allied World is delivering great results again in 2023 (after having a stellar 2022)

- To Sept 30, CR = 90.6%, UW profit = $318.5 million and net premiums written were +10.2% to $3.88 billion.
- To be fair, most of Fairfax's insurance subsidiaries are having a very good year. There is a good chance Fairfax could deliver a company-wide CR under 94% for 2023.

4.) The value (stock price) of Fairfax's position in Eurobank increased about $715 million in 2023.

- Over the past three years, the position is up $1.33 billion.
- Eurobank earnings spiked higher in 2022 and again in 2023.
- The company has solid growth prospects; the pending acquisition of Hellenic Bank will be a catalyst in 2024.
- Dividend will likely be re-instated in early 2024 and this should be supportive of the stock price.
- Fairfax's decision to merge Grivalia Holdings into Eurobank in 2019 is looking especially brilliant. With hindsight, the move allowed Fairfax to sell high (Grivalia) and buy low (Eurobank). At the time, the transaction was good for both parties.

Fairfax & Eurobank: 3-Year Performance				Annual	
1,166mn shares	Stock Price		Value of	Change in Value	
	Euro	US$	Position	$	%
Dec 31, 2020	€ 0.579	$0.639	$745	n/a	n/a
Dec 31, 2021	€ 0.891	$0.985	$1,148	$403	54%
Dec 31, 2022	€ 1.055	$1.166	$1,359	$211	18%
Dec 31, 2023	€ 1.610	$1.779	$2,074	$715	53%
Three Year Gain in Value				**$1,329**	**230%**

5.) <u>The value of Fairfax's position in FFH-Total Return Swaps increased $640 million in 2023</u>(giving it exposure to 1.96 million Fairfax shares).

- Since inception (basically three years), the position is up $1.07 billion.
- Fairfax shares continue to look very cheap, which suggests this position could continue to perform well for Fairfax.

Fairfax - Total Return Swap	FFH Share	TRS Market	Annual Increase in Value	
1.96 mill shares	Price	Value	US$	/share
Q4 '20/Q1 '21	$373	$731	n/a	n/a
Dec 31, 2021	$492	$965	$233	$10
Dec 31, 2022	$594	$1,164	$200	$9
Dec 21, 2023	$921	$1,805	$640	$28
Three Year Gain in Value			**$1,074**	**$46**
Position put on Q4-2020 and Q1-2021; Avg cost = $373/sh.				

6.) <u>Estimated increase in net premiums written in 2023 of $1.4 billion or 6% to $23.7 billion.</u>

- The hard market in P/C insurance that started in late 2019 continued in 2023.
- Over the last three years, net premiums written have increased $9 billion or 61%.
- For some perspective, Warren Buffett purchased P/C insurer Alleghany in 2022 for $11.2 billion. In 2022, Alleghany had <u>gross</u> premiums written of $8.5 billion.
- The growth Fairfax has experienced the past three years in net premiums written has increased the intrinsic value of the company considerably.

Fairfax: Change in Net Premiums Written			
	NPW	YOY	
	US$bn	Change	increase over past 36 months
2020	$14.7	n/a	
2021	$17.8	21%	
2022	$22.3	25%	
2023E	$23.7	6%	61%

7.) <u>Purchase of KIPCO's 44.3% interest in Gulf Insurance Group, increasing Fairfax's stake from 43.7% to 90%.</u>

- Cost? Aggregate fair valuation consideration of approximately $740 million (upfront payment of around $177 million and then 4 equal annual payments of $165 million).
- Prem on Fairfax Q1, 2023 Conference Call: "We structured it (the deal) in a way that perhaps a lot of it (annual payments) will come from the company itself, dividends from the company."
- Size of GIG (2022): Net premiums written of $1.7 billion and investments of $2.4 billion.
- Deal closed in December. In Q4, Fairfax will book a pre-tax gain of around $290 million.

- Fairfax goes from being a minority shareholder in GIG to the controlling shareholder.
- Strategically, this secures Fairfax's position as one of the leading P/C insurance providers in the Middle East North Africa (MENA) region.
- Fairfax is using its substantial cash flow to grow its insurance operations. It is also buying more of something it already owns (and knows well), a capital allocation strategy endorsed by both Peter Lynch and Warren Buffett.

8.) <u>Purchase of $1.8 billion of PacWest real estate loans with expected annual return of 10%.</u>

- This was one of Fairfax's big capital allocation decisions of 2023; very contrarian, very opportunistic and deep value.
- Expansion of real estate/debt platform partnership with Kennedy Wilson (to over $4 billion in total).
- Fairfax also invested $200 million directly in KW in debentures (6%) with 7-year warrants (12.3 million shares with strike price of $16.21).
- In December, it appears Fairfax increased their commitment to the KW debt platform by $2 billion from $8 billion to $10 billion. This will be something to monitor in 2024.

9.) <u>The market value of Fairfax's position in Thomas Cook India (TCIL) increased about $305 million in 2023.</u>

- The excess of market value to carrying value (at Sept 30) increased by about $379 million. A significant portion of the value of TCIL is not captured in Fairfax's book value (about $338 million at YE).
- On December 1, Fairfax sold 40 million shares for proceeds of $67 million.
- Covid hit TCIL especially hard. TCIL (and Sterling Resorts) aggressively cut costs. With its travel businesses rebounding strongly in 2023, the much lower cost base is now spiking profits.

Fairfax and Thomas Cook India							
Year-Over-Year Change in Value of Position					**Carrying Value**	**Excess MV to CV**	
	Shares mn	**Market Value INR**	**US$**	**Total $**	**Total $**	**Total $**	
Dec 31, 2022	340.4	₹ 71.15	$0.85	$290	$214	$76	
Dec 31, 2023	300.3	₹ 146.70	$1.76	$528	$191	$338	Carrying value at Sept 30
Sale Dec 1	40.0		$1.67	$67	$25	$41	Carrying value at Sept 30
Total 2023 value				**$595**	**$216**	**$379**	
YOY Increase in Value of Total Position				**$305**			

10.) <u>Monetized another asset and booked a $275 million pre-tax investment gain</u> (closed in Q2, 2023).

- Sale of Ambridge Group (MGU operations of Brit) to Amynta Group for $379 million (and an additional $100 million subject to 2023 performance targets).
- Fairfax also entered into multi-year strategic partnership with Amynta

Asset sales are important part of capital allocation framework at Fairfax, and this is something that differentiates it from BRK and Markel.

Why sell an asset? Someone values it much more and/or for strategic reasons (the asset is a better fit elsewhere).

<u>Accounting Change</u>:

<u>Implementation of IFRS 17 accounting standard Jan 1, 2023, increase BV per share by $104.60.</u>

- On January 1, 2023, Fairfax (and all Canadian insurers) were required to implement IFRS 17 accounting standard. The cumulative effect of implementing IFRS 17 resulted in an increase in common shareholders' equity at Fairfax of $2.4 billion at December 31, 2022.
- Pre-IFRS 17, at December 31, 2022, BV/share was US$658.
- Post-IFRS 17, at December 31, 2022, BV/share was US$762.
- Below is what Fairfax had to say about IFRS 17 when they released Q1, 2023 results:

Adoption of IFRS 17
Insurance Contracts
("IFRS 17") on January 1, 2023

On January 1, 2023 Fairfax adopted the new accounting standard for insurance contracts (IFRS 17).

- It resulted in considerable changes to the recognition, measurement, presentation and disclosure of the company's insurance and reinsurance operations – the most significant being the discounting of the company's net insurance liabilities and a new risk adjustment for uncertainty.
- This new accounting standard has not changed the way management evaluates the performance of its property and casualty insurance and reinsurance operations. The company remains focused on underwriting profit on an undiscounted basis with strong reserving with all of the property and casualty insurance and reinsurance operations continuing to use the traditional performance measures of gross premiums written, net premiums written and combined ratios to manage the business.
- The cumulative effect of implementing IFRS 17 was $2.4 billion and was recognized as an increase in common shareholders' equity at December 31, 2022 (an increase in book value per share of $104.60), primarily reflecting the introduction of discounting net claims reserves of $4.7 billion, partially offset by a risk adjustment of $1.6 billion for uncertainty related to the timing and amount of cash flows from non-financial risk and by the tax effect of the measurement changes and other of $0.7 billion.
- The new standard increased common shareholders' equity at December 31, 2022 to $17.8 billion, a book value per share of $762.28.

<u>Honourable mention</u>:

- Digit - growth of the business during the year was solid.
- BIAL - back in growth mode. Fairfax India purchased another 10% for $250 million.
- Increase in value of Mytilineos share price.
- Turnaround at Brit? After a couple of years of underperformance (from an underwriting perspective) it looks like Brit might have turned the corner in 2023.
- Reduction in size of Blackberry debenture to $150 million (to Feb 14, 2024), down from $365 million (was $500 million in 2020). Capital is being re-allocated from under-performers to better opportunities.

- I estimate Fairfax will reduce shares outstanding by about 1% in 2023. This is at a slower pace than the past couple of years. Over the past three years, the share count has been reduced by 3.06 million shares or 11.7%, at an average cost of US$508. My guess is Fairfax's BV will finish 2023 north of US$900. This is yet another example of excellent capital allocation by Fairfax.

Fairfax - Reduction In Shares Outstanding - Last 3 Years				
Date	Effective Shares Outstanding million	Share Reduction million	Avg Cost Per Share	Total Cost US$ bn
Dec 31, 2020	26.176	n/a	n/a	n/a
Dec 31, 2021	23.866	2.310	$490	$1.132
Dec 31, 2022	23.325	0.541	$509	$0.275
Sept 30, 2023	23.116	0.209	$698	$0.146
Totals	**-11.7%**	**3.060**	**$508**	**$1.553**

Incomplete:

- Meadow Foods (UK): how much did Fairfax spend to purchase a majority position in August? What are prospects of the company? (Company had £550 million in sales…)

Negatives:

- Continued decline in prospects of Blackberry/share price (market value of Fairfax's position is down to $165 million at Dec 31, 2023).
- End of Farmers Edge: Fairfax is trying to take company private (to harvest significant tax losses?).
- Adverse reserve development in runoff of $80 million in 1H. Something to monitor moving forward.
- Digit IPO: in 2023, company appeared to continued to fumble the ball with regulators in India.
- Digit - still waiting for clarity on compulsory convertible preferred shares (expected to take Fairfax's ownership position from 49% to 74%); appears to be another issue with regulators in India.

Personnel announcements:

- January 2023 Fairfax news release: "Brian Young, CEO of Odyssey Group, will begin to share oversight responsibilities with Andy Barnard, President of Fairfax Insurance Group, over all of Fairfax's insurance and reinsurance operations. Brian Young will continue as CEO of Odyssey Group."

Chapter 15: What Are Others Writing?

Articles on Fairfax

Edgepoint Wealth (January 2023)

Below is a link to a well written summary from Edgepoint Wealth of the current opportunity with Fairfax.

- Provides a concise, easy to understand history of Fairfax that bridges nicely to where the company is at today. This is not easy to do with Fairfax.
- Identifies Fairfax as a GROWTH company.

https://www.edgepointwealth.com/article/Q4-2022-EdgePoint-commentary/

Woodlock House Family Capital – The Horse Story (2019)

I love the 'horse story.' Written back in 2019, the short write up is well done and still applicable today. The author provides a nice 'rule of thumb' way to value an insurance stock.

https://www.woodlockhousefamilycapital.com/post/the-horse-story

Articles on a Fairfax Holding

Tidefall Capital LP - Fairfax India (Jan 2023)

Concise summary of the opportunity with Fairfax India.

https://www.tidefallcapital.com/_files/ugd/8a849d_f70eefd143454bdab61ed5a4357dee37.pdf

Fairway Reasearch - Valuing BIAL, Fairfax India's Crown Jewel (Jan 2023)

"Bangalore International Airport's intrinsic value and implications on FIH NAV discount"

https://www.fairwayresearch.com/p/valuing-fairfax-indias-crown-jewel

Podcasts on Fairfax and/or the P/C Insurance Industry

The Templeton Way: Investing in P/C Insurance Companies with Nick Martin

Podcast: The Templeton Way
Title: Investing in Insurance Companies: Dynamic Compounding Opportunities with Nick Martin
Date: September 20, 2023
Host: Lauren Templeton – Sits on Board of Directors at Fairfax
Guest: Nick Martin – Polar Capital (collaborative meritocracy – focussed on performance not assets)

Podcast Link: https://podcasts.apple.com/ca/podcast/investing-the-templeton-way/id1604395168?i=1000628581359

Overview: Nick has been investing in insurance companies for over 25 years. He provides a great overview of the P/C industry from an investor's perspective. Many current topics are discussed. Polar was a shareholder of Fairfax on the date of the podcast.

Note: the podcast is not specifically about Fairfax.

Polar Capital Global Insurance Fund Fact Sheet (for UK investors):
https://www.polarcapital.co.uk/srp/lit/XGGalE/Fund-Data-Fact-Sheet_Polar-Capital-Funds-plc-Global-Insurance-Fund-R-Acc-GBP_31-08-2023_Multi-Audience.pdf

The Templeton Way: Ben Watsa - His Journey; Investing in India; Fairfax's Culture

Podcast: The Templeton Way
Title: Rising Star: Ben Watsa's Views on India, Fairfax and Beyond
Date: September 12, 2023
Host: Lauren Templeton – Sits on Board of Directors at Fairfax
Guest: Ben Watsa – President of Marval Capital Ltd. Also sits on Board of Directors at Fairfax.

Podcast Link: https://podcasts.apple.com/ca/podcast/investing-the-templeton-way/id1604395168?i=1000627607421

Overview: Ben Watsa is the son of Prem Watsa, the Chairman, CEO and founder of Fairfax. Given Fairfax is a family controlled company, and Prem is over 70 years old, Ben will have a very important role to play at Fairfax in the future. The podcast provides Fairfax shareholders with a good introduction to Ben. Topics discussed include his personal journey and investing in India.

Fairfax is discussed at the 53:45 mark: culture and family control.

The Business Brew: Fairfax is a "Fat Pitch" with Charlie Frischer and Asheef Lalani

Podcast: The Business Brew – Bill Brewster
Title: Fairfax is a "Fat Pitch"
Date: July 20, 2023
Host: Bill Brewtser
Guests: Charlie Frischer and Asheef Lalani

Podcast Link: https://podcasts.apple.com/ca/podcast/the-business-brew/id1540847053?i=1000621753971

Overview: Charlie is a long term Fairfax shareholder (+20 years) and Asheef is a more recent investor in Fairfax (2021). Both are very knowledgeable on the company. Bill's questions start focussed on Fairfax's past: trust in management, reserving and past equity investments. Charlie and Asheef do a good job of bridging the discussion to Fairfax as it exists today, including its cheap valuation and its solid future prospects.

AM Best Upgrades Credit Rating of Fairfax / Allied World / Odyssey

July 8, 2023

Who is AM Best?

AM Best is the largest credit agency in the world specializing in the insurance industry. It is the gold standard for insurance companies. AM Best looks at two broad buckets:

1. Long-Term Issuer Credit Rating (ICR): "an independent opinion of an entity's ability to meet its ongoing financial obligations" for unsecured debt and preferred equity.
2. Financial Strength Rating (FSR): "an independent opinion of an insurer's financial strength and ability to meet its ongoing insurance policy and contract obligations."

What did we learn?

Fairfax, Allied World and Odyssey Group all have had their credit ratings upgraded in recent months on improved financials at parent Fairfax. This is further confirmation that the progress we have seen at Fairfax over the past 5 years is being recognized (and rewarded) by other external organizations, like AM Best.

Long-Term ICR:

- Fairfax upgraded to "bbb+" (Good) from "bbb" (Good).
- Allied World upgraded to "a+" (Excellent) from "a" (Excellent)
- Odyssey Group upgraded to "aa-" (superior) from "a+" (Excellent)
- For comparison, WR Berkley is "a-" (Excellent) and Markel is "bbb+" (Good).

Financial Strength Rating:

- Allied World affirmed at "A" (Excellent) – no change
- Odyssey Group upgraded to "A+" (Superior) from "A" (Excellent)
- For comparison, WR Berkley is "A+" (Superior) and Markel is "A" (Excellent)

AM Best Upgrades Fairfax and Allied World – May 3, 2023

"The Long-Term ICR upgrade for Fairfax reflects its ability to limit investment volatility through year-end 2022, and the prospective earnings outlook from deploying substantial cash into higher yielding debt instruments. Fairfax has benefited from solid underlying returns among its core operating subsidiaries in recent years, despite elevated catastrophic losses in the North American market. **Furthermore, due to its relatively low duration and strong cash position at year-end 2021, Fairfax's unrealized losses from the market turmoil in 2022 were materially less than peer averages**. The upgrade also considers that Fairfax's financial leverage has improved materially compared with historically higher levels and has been consistently maintained at levels largely in line with comparably rated peers in recent years. AM Best expects that Fairfax will continue to maintain financial leverage at or near current levels going forward. The group's capital position should continue to improve over time, as it benefits from higher levels of dividend and interest incomes, which should further reduce the group's reliance on external debt."

https://www.businesswire.com/news/home/20230503005889/en/AM-Best-Upgrades-Issuer-Credit-Ratings-of-Fairfax-Financial-Holdings-Limited-Its-Subsidiaries-and-Allied-World-Assurance-Company-Holdings-Ltd

AM Best Upgrades Odyssey Group – July 6, 2023

"**The rating upgrades recognize the removal of ratings drag from Odyssey Group's parent company, Fairfax Financial Holdings Limited (Fairfax), which has demonstrated sustained improvement in its overall credit profile in recent years.** Fairfax has reduced its debt leverage materially and improved its overall operating performance, while maintaining consistently sound balance sheet strength and financial flexibility. As a result, debt servicing metrics have improved sustainably, reducing the burden imposed on Fairfax subsidiaries and supporting the removal of ratings drag on Odyssey Group."

https://www.businesswire.com/news/home/20230706093283/en/AM-Best-Upgrades-Credit-Ratings-of-Odyssey-Group-Holdings-Inc.'s-Members

Why the upgrade for Odyssey?

- balance sheet strength, which AM Best assesses as strongest
- strong operating performance
- favorable business profile
- appropriate enterprise risk management

AM Best's definitions:

GUIDE TO BEST'S ISSUER CREDIT RATINGS – (ICR)

A Best's Issuer Credit Rating (ICR) is an independent opinion of an entity's ability to meet its ongoing financial obligations and can be issued on either a long- or short-term basis. A Long-Term ICR is an opinion of an entity's ability to meet its ongoing senior financial obligations, while a Short-Term ICR is an opinion of an entity's ability to meet its ongoing financial obligations with original maturities generally less than one year. An ICR is an opinion regarding the relative future credit risk of an entity. Credit risk is the risk that an entity may not meet its contractual financial obligations as they come due. An ICR does not address any other risk. In addition, an ICR is not a recommendation to buy, sell or hold any securities, contracts or any other financial obligations, nor does it address the suitability of any particular financial obligation for a specific purpose or purchaser. An ICR may be displayed with a rating identifier or modifier that denotes a unique aspect of the opinion.

Best's Long-Term Issuer Credit Rating (Long-Term ICR) Scale

Rating Categories	Rating Symbols	Rating Notches*	Category Definitions
Exceptional	aaa	-	Assigned to entities that have, in our opinion, an exceptional ability to meet their ongoing senior financial obligations.
Superior	aa	aa+ / aa-	Assigned to entities that have, in our opinion, a superior ability to meet their ongoing senior financial obligations.
Excellent	a	a+ / a-	Assigned to entities that have, in our opinion, an excellent ability to meet their ongoing senior financial obligations.
Good	bbb	bbb+ / bbb-	Assigned to entities that have, in our opinion, a good ability to meet their ongoing senior financial obligations.
Fair	bb	bb+ / bb-	Assigned to entities that have, in our opinion, a fair ability to meet their ongoing senior financial obligations. Credit quality is vulnerable to adverse changes in industry and economic conditions.
Marginal	b	b+ / b-	Assigned to entities that have, in our opinion, a marginal ability to meet their ongoing senior financial obligations. Credit quality is vulnerable to adverse changes in industry and economic conditions.
Weak	ccc	ccc+ / ccc-	Assigned to entities that have, in our opinion, a weak ability to meet their ongoing senior financial obligations. Credit quality is vulnerable to adverse changes in industry and economic conditions.
Very Weak	cc	-	Assigned to entities that have, in our opinion, a very weak ability to meet their ongoing senior financial obligations. Credit quality is very vulnerable to adverse changes in industry and economic conditions.
Poor	c	-	Assigned to entities that have, in our opinion, a poor ability to meet their ongoing senior financial obligations. Credit quality is extremely vulnerable to adverse changes in industry and economic conditions.

GUIDE TO BEST'S FINANCIAL STRENGTH RATINGS – (FSR)

A Best's Financial Strength Rating (FSR) is an independent opinion of an insurer's financial strength and ability to meet its ongoing insurance policy and contract obligations. An FSR is not assigned to specific insurance policies or contracts and does not address any other risk, including, but not limited to, an insurer's claims-payment policies or procedures; the ability of the insurer to dispute or deny claims payment on grounds of misrepresentation or fraud; or any specific liability contractually borne by the policy or contract holder. An FSR is not a recommendation to purchase, hold or terminate any insurance policy, contract or any other financial obligation issued by an insurer, nor does it address the suitability of any particular policy or contract for a specific purpose or purchaser. In addition, an FSR may be displayed with a rating identifier, modifier or affiliation code that denotes a unique aspect of the opinion.

Best's Financial Strength Rating (FSR) Scale

Rating Categories	Rating Symbols	Rating Notches*	Category Definitions
Superior	A+	A++	Assigned to insurance companies that have, in our opinion, a superior ability to meet their ongoing insurance obligations.
Excellent	A	A-	Assigned to insurance companies that have, in our opinion, an excellent ability to meet their ongoing insurance obligations.
Good	B+	B++	Assigned to insurance companies that have, in our opinion, a good ability to meet their ongoing insurance obligations.
Fair	B	B-	Assigned to insurance companies that have, in our opinion, a fair ability to meet their ongoing insurance obligations. Financial strength is vulnerable to adverse changes in underwriting and economic conditions.
Marginal	C+	C++	Assigned to insurance companies that have, in our opinion, a marginal ability to meet their ongoing insurance obligations. Financial strength is vulnerable to adverse changes in underwriting and economic conditions.
Weak	C	C-	Assigned to insurance companies that have, in our opinion, a weak ability to meet their ongoing insurance obligations. Financial strength is very vulnerable to adverse changes in underwriting and economic conditions.
Poor	D	-	Assigned to insurance companies that have, in our opinion, a poor ability to meet their ongoing insurance obligations. Financial strength is extremely vulnerable to adverse changes in underwriting and economic conditions.

* Each Best's Financial Strength Rating Category from "A+" to "C" includes a Rating Notch to reflect a gradation of financial strength within the category. A Rating Notch is expressed with either a second plus "+" or a minus "-".

Chapter 16: Education / Information on P/C Insurance Industry

Investors have a variety of great resources at their access to learn about the P/C insurance industry. Below are just a few sources that may be of interest. Listening to the earnings conference calls of other P/C insurers (like WR Berkley or Chubb), especially the Q&A part, can be a good way to learn about current conditions.

Education

AM Best's Guide to Understanding the Insurance Industry

"…designed to be a gentle and broad introduction to the industry for students, new employees, prospects and those who would like to learn more about one of the most interesting and important financial services industries."

https://bestsreview.ambest.com/edition/2024/January/

2024 Outlook

Swiss Re Institute: US P/C Outlook: strong momentum into 2024, led by personal lines

https://www.swissre.com/institute/research/sigma-research/Insurance-Monitoring/us-property-casualty-outlook-january-2024.html#:~:text=We%20raise%20our%20premium%20growth,offset%20by%20weak%20liability%20growth.

Current Information Websites

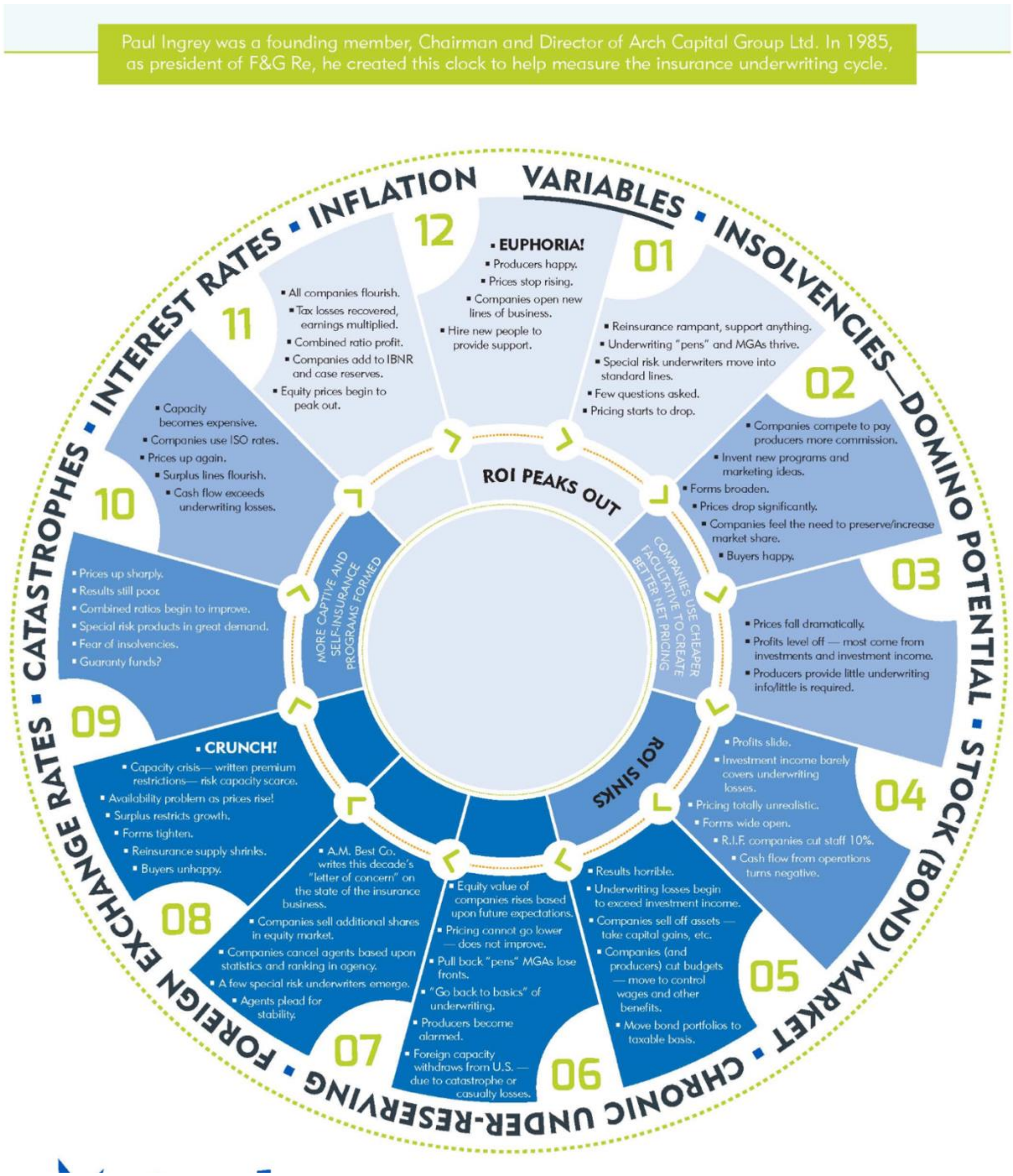
Good comprehensive site: https://www.reinsurancene.ws

Canadian perspective: https://www.canadianunderwriter.ca

Paul Ingrey's Insurance Clock

Of interest, Paul served on Fairfax's board in 2001/02 (stepping down due to his role at Arch).

<u>The underwriting life cycle</u>: https://www.archgroup.com/the-underwriting-lifecycle/
Creating shareholder value through the insurance cycle has been central to the company's management philosophy since Arch was established in 2001. We don't chase unprofitable business in soft markets, but we do write more business as attractive opportunities arise in hard markets.



Where are we in the insurance cycle? Arch CEO Q2 Comments on Paul Ingrey's Insurance Clock

July 27, 2023

Arch Capital's CEO Marc Grandisson comments during Q2, 2023 conference call on where the P/C insurance market currently is at in the insurance cycle. He references the 'insurance clock,' a model created by Paul Ingrey (also of Arch). See the next page for a more complete summary of Paul's work.

"This hard P&C market is proving to be one of the longest we've experienced and we are in an enviable position as we look to 2024 and beyond.

"We often refer to the insurance clock developed by to help illustrate the insurance cycle. You can find the clock on the download cap for this webcast or on our corporate website. If you can't do the clock right now, just picture a traditional clock dial. For some time, we've been hovering at 11:00, which is one we expect most companies in the market to show good results as rate adequacy improves and loss trends stabilize.

"Last year, a popular topic on earnings calls was whether rate increases were slowing or what the rates were even decreasing. These are classic signs of the clock hitting 12 when returns are still very good, but conditions begin to soften. Yet here we are in mid-2023 and conditions in most markets remain at 11:00. We've even checked the batteries in the clock and they're just fine. The clock isn't broken. It's just that the current environment dictates an extended period of rate hardening.

"So, what's sustaining this hard market? Well, I believe it's a relatively simple combination. Heightened uncertainty is driving an imbalance of supply and demand for insurance coverage. Since this hard market inception in 2019, we've had COVID to war in Ukraine, increased cat activity and rising inflation, all of which create significant economic uncertainty. Underwriters have had to account for more unknowns. Beyond those macro factors, industry dynamics also play a role in sustaining the hard market. Generally, in adequate pricing and overly optimistic loss trend assumptions during the soft market years of 2016 through 2019 have led to inadequate returns for the industry.

"The impact of these factors should cause insurers to raise rates and purchase more reinsurance in a capacity-constrained market with limited new capital formation. Put it all together, and it may be a while before the clock strikes 12 and we begin to move beyond this hard market."

Appendix: Summary of Asset Purchases and Sales Going Back to 2010

What follows below is a detailed compilation of Fairfax's purchases and sales (insurance and investments) for each year going back to 2010. It is long – at nine pages. It provides good insight into how capital allocation at Fairfax has changed over the years – especially with their equity holdings. Their track record with new purchases since 2018 has been outstanding.

	Fairfax Transaction Summary						
	How the legacy insurance companies were formed (from 2016 AR)						
1985	**Markel Insurance**			$10			
1989	Federated Insurance			$29			
1990	Commonwealth Insurance			$58			
1994	Lombard Insurance			$155			Northbridge was golden goose in early years that propelled expansion
2003	Northbridge Insurance	created from 4 listed above					Total investment $252 million
1995	Skandia US (renamed **Odyssey Re**)			$228			BV $314
1996	CTR						
1999	TIG Re						
2002	Hudson expansion	created core of Odyssey Re					
1998	**Crum & Forster**			$680			
2000	Seneca			$65			
2006	Fairmont (from TIG)						
2011	First Mercury			$294			
	Redwoods Group, Travel Insured, Brownyard Programs and Trinity Risk						2016 AR: Crum has paid most dividends of all insurance co's
	A Few Transactions From Before 2010						
2001	ICICI Lombard	Minority partner					Partner with ICICI Bank
2002	First Capital (Singapore)	New insurance buy		$35			
06 to 09	International Coal Group #1					$152	Chairman of IC was Wilbur Ross; p8 2011 AR
2008	Abitibi (Resolute)	New debt buy				$347	Convertible bond
08 & 09	Sandridge Energy	Primarily convertible preferds				$329	Invested Q3 2008 & Nov 2009
2009	BDT Capital	Initial investment					
			Insurance		**Non-Insurance**		
			Sale	**Buy**	**Sale**	**Purchase**	
Date	**2010**	All figures are US$	**Proceeds**	**Cost**	**Proceeds**	**Cost**	**Comments**
30-Mar	Mega Brands (Can) #1	Recapitalization					Fairfax owns 16.5% (does warrants bump this up to 31%?)
12-May	SFK Pulp (Can)	Add to position					SFK Pulp becomes Fibrek; Fairfax owns 20.38%
20-May	Zenith National (US)	Insurance buy		$1,300			Fairfax owns 100%; prior to acquisition Fairfax had owned 8.2%
01-Jul	TIG Indemnity	Insurance sale					Realized net gain before taxes of $7.5 million
16-Jul	Fibrek (Can) was Abitibi	Add to position				$16	Fairfax owns 25.8%
20-Aug	General Fidelity - GFIC (US)	Runoff buy		$241			First runoff acquisition; part of Riverstone
28-Sep	Gulf Insurance Group (Middle East)	New insurance buy		$217			Fairfax owns 41.3%; partners with KIPCO
28-Sep	Arab Orient	Insurance sale	$11				Sold to GIG at cost (purchased in 2008)
10-Dec	International Coal Group #2	Sell down position			$164		After sale owns 11.1%. Investment gain = $77.9 million
	Kennedy Wilson (US)	New equity buy				$100	6% preferred converible @ $12.41/share
	Fairfax owns 18.5% of KW					$33	6.56% preferred convertible @ $10.70/share
	In 2010 & 2011 invested $290 million in real estate deals with KW					$4	400 thousand shares @ $10.70/share
	Magna (Can)				$99		realized gain amount (+62%)
	General Electric				$51		realized gain amount (+13%)
	Cheung Kong				$26		realized gain amount (+50%)
	Equity hedges					$937	Unrealized losses = cost 4.2% in total return in 2010
	CPI-linked derivative contracts				$28		Unrealized gain. YE value = $328.6; avg term 9.4 years
		Total 2010	**$11**	**$1,758**	**$368**	**$1,089**	

			Insurance		Non-Insurance		
			Sale	Buy	Sale	Purchase	
Date	**2011**	All figures are US$	Proceeds	Cost	Proceeds	Cost	**Comments**
04-Jan	GAB Robins North America	Insurance buy					Provider of loss adjusting and claims management services
09-Feb	First Mercury (US)	Insurance buy		$294			Fairfax owns 100%
24-Mar	Pacific Insurance (Malaysia)	Insurance buy		$72			Fairfax owns 100%
29-Jun	The Brick (Can)	Add to position				$88	Exercise of warrants; Fairfax increased ownership from 17.3 to 33.6%
30-Jun	RIM / Blackberry (Can) #1	New equity buy					At June 30 Fairfax owned 241,340 shares valued at $8.4 million (13F)
26-Jul	Bank of Ireland #1	New equity buy				$387	Fairfax owns 8.7%. (2.8 billion shares at €0.10/share). Consortium with Will
16-Aug	William Ashley (Can)	New equity buy					
30-Sep	International Forest Products (Can)						Fairfax owns 18.85%
21-Nov	Mega Brands #2	Add to position					Fairfax buys 500,000 common shares; including warrants owns 32.3%
22-Dec	Sporting Life (Can)	New equity buy				$31	Fairfax owns 75%
29-Dec	Imvescor Restaurant Group (Can)	Recapitalization				$10	If warrants exercised Fairfax owns 37.8%
30-Dec	Polskie (PTU)	Sold all of position				$10	Gain on sale of $7 million
31-Dec	ICICI Lombard Ins (India) #1	Add to position		$108			To acquire and maintain 26% interest; fair value = $230.4 million
	Grivalia-Euobank Prop (Greece) #1	New equity buy					In 2011 Fairfax purchases intial position of 3.8% for ?
	International Coal Group #3	Exit position			$330		Total realized gain on ICG = $341.2 million (sold in 2 tranches in 2010 and 2(
	Kraft	Exit position			$385		Cost = $291 million. Realized gain = $94 million = 32%. Bought Q1 2009
	Equity hedges				$414		Unrealized gain
	CPI-linked derivative contracts					$234	Unrealized loss
		Total 2011	**$0**	**$474**	**$1,129**	**$760**	
			Insurance		Non-Insurance		
			Sale	Buy	Sale	Purchase	
Date	**2012**	All figures are US$	Proceeds	Cost	Proceeds	Cost	**Comments**
10-Jan	Prime Restaurants (Can)	New equity buy				$69	Fairfax owns 81.7%
27-Jan	RIM / Blackberry #2	Add to position					Raised stake to 5.12%; owns 26.85 million shares up from 11.8 million
19-Mar	Thai Re (Thailand)	Add to position		$77			Fairfax ownership from 2% to 23.2%; opportunistic (after tsunami)
2012	Thomas Cook (India)	New equity buy				$173	Fairfax owns 87.1%; "vehicle for expansion in India"
Aug	Grivalia (Eurobank Properties) #2	Add to position				$50	Fairfax ownership increases from 3.8% to 18%
Sept	Mullen Group (Can)	Exit position			$136		Cost C$65 milion in 2009 (10% convertible debentures)
12-Oct	Brit Insurance (UK)	Runoff buy		$335			Fairfax owns 100%;
01-Nov	Imvescor Restaurant Group	Add to position				$1	If warrants exercised, Fairfax owns 45%
11-Nov	The Brick (see Leon's)	Merger			$221		Sold to Leon's; realized gain = $112 million (early 2013)
	Leons Furniture (Can)						Fairfax's ownership in new company?
10-Dec	Cunningham Lindsey	Insurance Sale			$271		Recognized net gain of $167 million.
	Arbor Memorial (Can) #1	Take private				$105	Fairfax holds 39.5% interest ($88 million gain on sale of public shares?)
	Alliance Insurance (Turkey?)						Sale to GIG
	Equity hedges					$1,006	Unrealized loss
	CPI-linked derivative contracts					$129	Unrealized loss
		Total 2012	**$0**	**$412**	**$627**	**$1,532**	
			Insurance		Non-Insurance		
			Sale	Buy	Sale	Purchase	Average exchange rate CAN$ to US$ $0.971
Date	**2013**	All figures are US$	Proceeds	Cost	Proceeds	Cost	**Comments**
02-Apr	Imvescor Restaurant Group	Exit position			$26		Sold to GMP Securities
14-May	IKYA (India) / Quess #1	Private equity buy					Thomas cook acquired 77.3% for $46.8 million; became Quess; funded via pr
03-Jul	Hartville Group (US) - pet insurance	Insurance buy		$34			Crum & Forster purchased 100%
03-Oct	American Safety (US)	Insurance buy		$317			Fairfax received dividend of $123.7 million; some business run off
08-Oct	AS Re	Insurance sale	$53				America Safety's Bermuda based reinsurance sub
31-Oct	Prime Restaurants	Merger					81.7% interest to CARA in exchange for shares/warrants = $54.5 million
	Cara(Can) #1	New equity buy				$96	Fairfax owns 49% of CARA (total Cara investment = $ 157 million 2016 AR)
23-Sep	Blackberry	Take private					$4.7 billion deal did not happen. Only announced deal Fairfax walked away f
18-Oct	Mytilineos (Greece)	New equity buy				$41	Fairfax owned 5.9%; of total, Mytil said FFH buys 4.97 mill sh at €5.13 = €25
13-Nov	Blackberry #3	Debenture buy				$500	Debentures pay 6% & convertible at $10/share.
20-Dec	Reitmans (Can)	Add to position				$12	Fairfax owns 13.8% (was 9.9%); paid C$6.35/share for 2 million shares
	Eurobank Properties (Grivalia) #3	Add to position				$27	Fairfax owns 41%. Position had unrealized gain $109 million at YE 2013
	Wells Fargo	Exit position	sold to		$795		Cost = $388. Realized gain of $407 = 105% over life of holding
	J&J	Exit position	offset		$725		Cost = $512. Realized gain of $213 = 42% over life of holding
	US Bankcorp	Exit position	equity		$178		Cost = $258. Realized gain of $309 = 120% over life of holding
	USG	Exit position	hedge				Realized gain = $69
	Fiat	Exit position	losses				Realized gain = $69
	Jumbo	Exit position					Realized gain = $56
	Equity hedges					$1,982	Unrealized loss
	CPI-linked derivative contracts					$127	Unrealized loss
		Total 2013	**$53**	**$351**	**$1,724**	**$2,785**	

Date	2014	All figures are US$	Insurance Sale Proceeds	Insurance Buy Cost	Non-Insurance Sale Proceeds	Non-Insurance Purchase Cost	Comments
							Average exchange rate CAN$ to US$ $0.906
04-Feb	Keg (Can)	New equity buy				$77	Fairfax owns 51%
09-Feb	Thomas Cook	Add to position				$81	Fairfax contribution to help Thomas Cook purchase Sterling Resorts ($140 m
28-Feb	Mega Brands	Exit position					Sold to Mattel; Fairfax made $17 milllion (including loss on original debs)
04-Mar	Bank of Ireland #2	Sell down position			$342		€308 million (933 x €0.33). Fairfax owns 5.8% (down from 8.7%).
20-Mar	Torstar (Can)	Add to Torstar				$12	Fairfax owns 22.7%
May	CIB Bank (Egypt)	New equity buy				$330	Fairfax owns 7.3%. Great bank. Issue since initial purchase has been currenc
21-May	PT Batavia (Indonesia)	Insurance buy		$9			Fairfax owns 80%; renamed Fairfax Indonesia
05-Jun	Praktiker Hellas (Greece)	New equity buy				$29	Fairfax owns 100%; Home improvement/big box Greece; Grivalia owns som
30-Sep	IBM	New equity buy				$245	Q2 & Q3 13F: 1.36 million shares @ $180 (estimated cost)
14-Nov	Pet Health (Can)	Insurance buy		$89			Fairfax owns 100%. Paid 10 x free cash flow.
16-Dec	QBE insurance (Ukraine)	Insurance buy					Eastern European. Paid €9.75 million.
Dec	Eurobank (Greece) #1	New equity buy				$444	Fairfax spends €400 million; in 2015 became largest unrealized loss in Fairfa
	Equity hedges					$195	Unrealized loss
	CPI-linked derivative contracts				$18		Unrealized loss
		Total 2014	$0	$98	$360	$1,411	

Date	2015	All figures are US$	Insurance Sale Proceeds	Insurance Buy Cost	Non-Insurance Sale Proceeds	Non-Insurance Purchase Cost	Comments
							Average exchange rate Euro to US$ $1.11
							Average exchange rate CAN$ to US$ $0.7832
01-Jan	Union Unsurance (Sri Lanka)	Insurance buy		$28			Fairfax owns 78%; re-named Fairffirst Insurance; purchased from John Keell
01-Mar	MCIS Insurance (Malaysia)	Insurance buy		$13			Malaysian insurer
30-Jan	Fairfax India #1	IPO				$300	30 million shares @ $10/share; Fairfax owns 28%; 2014 Modi election in Inc
15-Mar	Bank of Ireland #3	Sell down position			$374		€313 = 935 shares x €0.36. Fairfax sold 1/2 of 5.8% stake for more than tripl
10-Apr	Cara #2	IPO					Fairfax owns 40.7% Exchanged existing holdings for common shares. Cara is
							C$230 million raised = $23 x 10 million
	Africa Re	Insurance		$61			7.2% stake
04-May	BIC Insurance Corp (Vietnam)	Insurance buy					Fairfax owns 35%; insurance sub of BIDV Bank, 2nd largest bank in Vietnam
05-Jun	Brit (UK) #1	Insurance buy		$1,657			Increased Lloyds profile of Fairfax. Issued 1.15 million Fairfax shares.
			$516				30% of Brit sold to OMERS
10-Jun	Tembec (Can)	New equity buy				$35	Fairfax owns 19.9%
18-Jun	Ridley	Exit position			$313		Sold its 73.6% interest; pre-tx gain = $236.4. Realized 31% annual gain.
24-Aug	Fairfax	Change to multiple voting share					Vote delayed twice; barely passed (required support of 2/3) by vote of 70%
05-Sep	The McEwan Group (Can)	New equity buy					Celebrity chef; owns 4 restaurants
Sept	FBD Group - Ireland	Insurance buy		$91			€70 million pounds; 10 year convertible bond. Leader in farm insurance
20-Oct	EXCO Resouces #1	Loan				$300	At 12.5%/year
30-Oct	ICICI Lombard #2	Add to position		$234			Bought 9%; Fairfax owns 34.6%. Partnership began 16 years ago. Total inves
Nov	Eurobank #2	Recapitalization				$389	Fairfax invests additional €350 million. Own inc from 12.5% to 17%
Nov	Quantum Advisors (India)					$46	Fairfax owns 49%; Invesmtnet manager
22-Dec	Eurolife (Greece) #1	Insurance buy		$181			Fairfax owns 40%; bought from Eurobank. 3rd largest insurer in Greece
							OMERS also bought 40% stake for $180 million
2015	Ambridge Partners #1	Insurance buy		$29			Brit purchases 50%; Ambridge (New York) is leading managing general ager
	IIFL Holdings (India)	Update on position				$65	Fairfax owns 8.97% and has economic interest of an additional 5.24%.
	Boat Rocker	Initial investment					Fairfax acquired controlling stake
	Farmers Edge #1	Initial investment					
	Colonade (Luxembourg)	Insurance					Created by Fairfax to write all Eastern European insurance business
	Equity hedges				$502		Unrealized gain
	CPI-linked derivative contracts				$36		Unrealized gain
	Share Issue						1.15 million shares issued to help buy Brit
		Total 2015	$516	$2,294	$1,224	$1,135	

Date	2016	All figures are US$	Insurance Sale Proceeds	Insurance Buy Cost	Non-Insurance Sale Proceeds	Non-Insurance Purchase Cost	Comments
							Average exchange rate CAN$ to US$ $0.7553
05-Jan	APR Energy (US) #1	Take private				$340	Fairfax owns 49% (was 18.9%). Total invested to date = $340 million. Total
31-Mar	Cara #3	Capital raise				$100	Fairfax owns 23.3 million shares = 39% euity & 57% voting. Help fund St Hul
16-May	Sandridge Energy	Bankruptcy (initial investment 2008)					Prem 2015AR: sounds like Fairfax lost 100% of investment. $329 million?
July	Quess #2	IPO					Quess raised $60 million selling 10% of company
Aug	Brit #2	Add to position					Brit paid $57.8; ownership increased to 73%
25-Aug	Torstar	Add to position				$5	Fairfax owns 27.4%
03-Oct	Asian Alliance (Sri Lanka)	Insurance buy		$10			Sri Lankan insurer; renamed Fairfirst insurance
10-Oct	AMAG Insurance (Indonesia)	Insurance buy		$179			Fairfax owns 80%
18-Oct	AIG Latin Am & East Europe	Insurance buy		$240			Built out Fairfax's Latin America and Central/Eastern Europe footprints
31-Oct	Golf Town (Can)	Bankruptcy purchase				$31	Fairfax owns 60%. 48 locations.
Oct/Nov	Fairfax	Before election sold 90% of treasury bonds (moved to cash)					US election / fundamental change / drmamtic improvement in US economy
		After election sells down equity hedges					"reduces the need for the capital preservation protection of equity hedging"
09-Dec	Bank of Ireland #4	Sell down position			$469		Proceeds 415 million Euros. Fairfax reduces ownership from 2.9% to 1.5%
07-Dec	Zurich South Africa (renamed Bryte)			$128			Renamed Bryte Insurance
19-Dec	Chorus Aviation (Can)	Debt & warrant deal				$155	Debs pay 6% + warrants strike $8.25; potentially own = 16.2%
	Davos Brands (US) #1	Private equity purchase				$50	35% interest with David Sokol
	Rouge Media (Can)	Private equity purchase					

	Blue Ant Media (Can)	Private equity purchase				$42	Debt and warrants
	Equity hedges					$1,193	2016AR: the presidential election on November 8, 2016 changed the world f
	CPI-linked derivative contracts					$196	Unrealized gain
	Share Issue						1 million to fund ICICI Lombard add and Eurolife buy
		Total 2016	**$0**	**$557**	**$469**	**$2,112**	
			Insurance		**Non-Insurance**		
			Sale	**Buy**	**Sale**	**Purchase**	
Date	**2017**	All figures are US$	**Proceeds**	**Cost**	**Proceeds**	**Cost**	**Comments**
13-Jan	Fairfax India #2	Second equity raise				$145	12.3 million shares @$11.75/share; Fairfax ows 30.2% of Fairfax India
26-Jan	Mosaic Capital Corp (Can)	Debt & warrant deal				$116	Debs pay 5.7% + warrants strike $8.81; potentially own = 61.7%
17-Feb	Fairfax Africa	IPO				$325	Paul Rivette was driver. Fairfax owns 64.2%; $252.2 cash + AFGRI (Fair valu
24-Feb	Altius (Can)	Debt & warrant deal				$78	Debs pay 5% + warrants strike $15.00; potentially own = 13.4%
01-Mar	Farmers Edge #2	Equity investment				$95	Fairfax owns 46.1%. Fairfax buys Kleiner Perkins stake.
	Farmers Edge	Debt and warrant deal				$64	Based on implied valuation of 4x projected Dec 2019 EBITDA
01-Mar	Performance Sports (Can) - Peak	Bankruptcy buy				$154	With Sagard Capital. 50% voting; equity 42.5%. Bauer, Easton, Cascade. Ren
15-Mar	EXCO Resources #2	1.5 Lein Notes				$151	Fairfax owns 9.9% of EXCO's common shares
		Exchanged to 1.75 Lien Term Loans					$412 million in value
10-May	Astarta Holdings (Ukraine)	New equity buy				$104	Bought via multiple transactions between Jan 3 and May 10.
27-May	ICICI Lombard #3	Sell down position #1	$376				Sell 12.18%; Fairfax owns 22%. Investment gain = $223.3 million
02-Jun	Westaim (Can)	Debt & warrant deal				$39	Debs pay 5% + warrants strike $3.25; potentially own = 8.2%
09-Jun	Tembec	Sell down position			$9		After sale Fairfax owns 17.4%
15-Jun	Tembec	Sell down position			$10		After sale Fairfax owns 14.2%
19-Jun	Tembec	Exit position			$47		Position exited
04-Jul	Grivalia Properties #4	Add to position				$100	Fairfax owns 52.6% an increase of 10.3%.
06-Jul	Allied World	Insurance buy		$4,900			Fairfax owns 67.4%. Paid 1.3 x BV. The company writes $3.1 billion in busine
			$1,560				OMERS, AIMCo, others own 32.5% for $1,580
20-Jul	APR Energy #2	Add to position				$109	Fairfax owns 67.9% (from 49%). Total invested = $340+109 = $449 million
25-Jul	AGT Food & Ingred (Can) #1	Debt & warrant deal				$148	Paul Rivette discovery. Debs pay 5.4% + warrants strike $33.25; potentially c
02-Aug	Sigma Companies International	New equity buy				$41	Fairfax owns 81.2%. Sigma engaged in global water and wastewater infrast
27-Sep	ICICI Lombard #4	Sell down position #2	$548				Sold 12.1%; Fairfax owns 9.9%. Investment gain = $372.1 million. ICICI Lomb
13-Oct	APR Energy #3	Add to position				$13	Capital raise; ownership fell slightly to 67.8%
09-Nov	Torstar	Add to position				$9	Fairfax owns 40.6% (increased position by 13.3%
23-Nov	Quess #3	Sell down position			$97		Thomas Cook reduces stake from 81.52 to 75.38
28-Dec	First Capital (Singapore)	Insurance sale	$1,683				Sold to Mitsui Sumitomo; after tax gain = $1,018.6. Compounded at 30% per
Dec	Go Digit (India) #1	Private equity buy		$11			Fairfax owns 45.3% equity interest
		Convertible preferred shares		$49			Sold ICICI position to 9.9%. Can't own > 10% of 2 insureres in India
30-Dec	IBM (initiated Q3 2014)	Exit position			$208		Sold Q2 to Q4 13F: 1.36 million shares X est $153/share
	Fairfax India #3	Add to position					Fairfax owns 33.6% from 30.2%. $114 million performance fee earned in sh
	TRG (Riverstone run-off)	Final Payment		$125			Final Payment as part of 2002 purchase. Riverstone was one of best acquisit
	Global small/mid cap fund	New equity buy				$50	Managed by Ben Watsa
	Bank of Ireland #5	Exit position					Sale of final 1.5%. Well over $1 billion in realized gains.
	Allied World	Underwriting loss		$587			Closed July 6; received only 6 months of premiums. Hurricanes Irma, Maria a
	Equity hedges					$418	Loss
	CPI-linked derivative contracts					$71	Loss
	Share Issue						5.1 milllion to fund Allied World acquisition
		Total 2017	**$4,167**	**$5,085**	**$371**	**$1,742**	
			Insurance		**Non-Insurance**		
			Sale	**Buy**	**Sale**	**Purchase**	Average exchange rate CAN$ to US$ $0.7717
Date	**2018**	All figures are US$	**Proceeds**	**Cost**	**Proceeds**	**Cost**	**Comments**
18-Jan	AIG Uruguay	Insurance buy		$6			Named SoughBridge Uruguay
14-Feb	Seaspan (Atlas) #1	Debt + warrants				$250	Debt pays 5.5%
	Tranche 1	Warrants					Warrants = 38.46 million shares ex @ $6.50; potentially own 22.4%
22-Feb	Keg / Cara	Merge with Cara			$8		51% interest sold to Recipe for $7.9 million + 3.4 million Recipe shares (Fair
		Cara changes name to Recipe					Fairfax 43.2%. Total Fairfax investment to date = $348 million
01-Mar	Quess #4	IPO					Thomas Cook deconsolidated Quess
							Fairfax remeasured caryling value to $1.1 bil; recog. gain = $889.9 mill
07-Mar	Carillion Canada (Dexterra) #1	Banrruptcy buy					Bought after Carillion UK declared bankruptcy; Renamed Dexterra (Canadian
09-Mar	Fairfax India #3	Performance fee					$114.4 million = 7.66 million Fairfax India shares; Fairfax owns 33.6% of Fai
12-Apr	Ensign Energe Services #1	Debt & warrant deal					
31-May	Toys "R" Us (Can)	Bankruptcy buy				$235	July
18-Jun	Fairfax Africa	Additional investment				$151	12.3 million shares @ $12.25/share
05-Jul	Brit (#3)	Add to position		$252			Purchased 11.2% stake from OMERS; Fairfax's ownership in Brit = 88%
16-Jul	Seaspan (Atlas) #2	Exercise of warrants (received in #1)				$250	Exercise of W received Feb 14, 2018: 38.46 mill shares at cost of $6.50
		Grant of new warrants					Issued new warrants = 25 mill shares @ $8.05/share as incentive to exercis
31-Aug	Sporting Life & Golf Town	Merger					Post merger Fairfax ows 65.1%
19-Nov	Stelco (Can) #1	New equity buy				$193	12.2 million shares @C$20.50/share. Fairfax owns 13.7%
	Eurolife #2	Add to position					Bought 10% from OMERS; Fairfax owns 50%
	Arbor Memorial #2	Exit position			$179		Realized gain = $111.8
	Equity hedges					$38	Loss
	CPI-linked derivative contracts						
		Total 2018	**$0**	**$258**	**$187**	**$1,117**	

Date	2019	All figures are US$	Insurance Sale Proceeds	Insurance Buy Cost	Non-Insurance Sale Proceeds	Non-Insurance Purchase Cost	Comments
							Average exchange rate CAN$ to US$ $0.7538
15-Jan	Seaspan (Atlas) #3	Debt + warrants				$250	Debt pays 5.5% + warrants = 38.46 million shares ex at $6.50
	Tranche 2	Exercise of warrants				$250	Fairfax owns 36%. Fairfax immediately exercised warrants. 38.46 million sh
14-Feb	AXA Ukraine	Insurance buy		$17			
17-Apr	AGT Food & Ingredients (#2)	Take private				$227	Including warrants Fairfax owns 80% of AGT
18-Apr	Ambridge Partners #2	Buy out by Brit					Brit acquired 50% equity it did not own for 46.6 million.
17-May	Grivalia #5 & Eurobank #3	Merger					Owned 53% Grivalia & 18% Eurobank; post owns 32.4% of Eurobank
28-Jun	EXCO Resources #3	Bankruptcy/Restructuring					Emerged from bankruptcy. Bonds exchanged for shares.
							Realized losses = $296 million; $179 in 2019 and $117 million prior years
01-Aug	Quess #5	Small add to position					Fairfax owns 32.35%
07-Aug	Reitmans	Exit position				$17	7.39 million shares x C$3
05-Nov	Universalna (Ukraine)	Insurance buy		$5			Merged with AXA to become Fairfax Ukraine
14-Nov	Avante Logixx	New equity position				$14	C$18 million invested in convertible debentures
19-Nov	APR #4	Sell to Atlas			$254		Fairfax got 22.9 million Atlas shares (@ $11.10) = $254 million
	Atlas #4						Post APR transaction Fairfax owns 99.9 million Atlas shares
Dec	Quess #6	Spin Off From Thomas Cook					Fairfax directly owns 33% of Quess
Dec	IIFL	Split into 3 companies					Finance, Wealth & Securities; also 5paisa
	ICICI Lombard #5	Exit position			$729		Sold final 9.9% stake. $311 million gain ($71 recorded in prior years so net g
	Stelco #2	Add to position					Fairfax owns 13 million shares (+800,000)
	Paul Rivette	Retires					Was responsible for many investments incl Fairfax Africa
	Equity hedges					$58	Loss
	CPI-linked derivative contracts						
		Total 2019	$0	$22	$983	$815	

Date	2020	All figures are US$	Insurance Sale Proceeds	Insurance Buy Cost	Non-Insurance Sale Proceeds	Non-Insurance Purchase Cost	Comments
							Average exchange rate CAN$ to US$ $0.7462
Jan	Digit	Capital raise					$91 mill raised for 10% of Digit from outside inv; values co at $858 million
							To date, Fairfax has invested $154 million (did not inv in $91 mill raise)
09-Jan	John Keells (Sri Lank Conglomorate)	New equity buy					The 10.76% stake in JKH amounting to 141.8 million shares was traded at R
Feb	Leon's Furniture						$48.5 million in convertible debentures converted to common shares
Feb	Atlas #5	Debt buy				$100	5.5%. Total debt = $600 million
31-Mar	Mastercraft (US)	New equity buy				$24	Q1 13F: 1.599 million shares X (guess) $15 (could be much lower)
31-Mar	Riverstone UK	Run-off insurance sale	$600				Joint venture with OMERS. Sold 40%. Fairfax owns 60%.
13-May	Ki (Brit) #1	Launch					Brit and Google Cloud collaborate to launch Ki (algo Lloyd's of London platfo
14-May	Kennedy Wilson	Real estate debt platform		$2,000			With Fairfax. $2 billion platform; KW will coinvest 20%. First mortgages We
26-May	Torstar	Exit position			$13		Fairfax booked US$52 mill loss. 28.9 million shares x C$0.63/share = C$18 m
29-May	Horizon North (Dexterra)	Reverse takeover					New company run by Dexterra. Fairfax owns 49% of new company
15-Jun	Ensign Energy Services	Add to position					Fairfax owns 10.76% of Ensign
16-Jun	Fairfax	Prem's big stock purchase					Prem spends $150 milion = 482,600 shares @ US$311/share
June	Eurobank	Cairo transaction					Eurobank's impaired loan ratio falls to 15.6%. €7.5 billion sold to doValue G
06-Aug	Omnia Media (owned by Blue Ant)	Sale to Enthusiast Gaming					Sold by Blue Ant Media for 18.25 million shares of Enthusiast Gaming +$11
02-Sep	Blackberry #4	Debenture redemption			$500		3.75%; convertible at $10 to shares (50 milion)
		Debenture purchase				$330	1.75%; convertible at $6 to shares (55 milion)
17-Sep	Ki #2	Capital raise		$100			$500 million from Blackstone and Fairfax (80/20 split?)
30-Sep	Lumen Technologies	New equity buy				$24	Q3 13F: 2.359 million shares X (guess) $10.10
Sept	Davos Brands #2	Exit position			$59		$59 + $36 million contingency payment
Oct	Paramount Health Services (India)					$11	Purchased by Fairfax Asia
Q3	Brit (#4)	Add to position		$206			Fairfax owns 100%; 30% bought in 3 transactions: $57.8+251.8+206.4=$516.
12-Nov	Vault Insurance	Sell down position					Fairfax continues to own 10% of Vault
30-Nov	Gulf Insurance Group	AXA acquisition					Adds $900 million in gross premiums to GIG's $1.4 million = $2.3 million
							Total cost was $474.75 million; Fairfax did not add $
08-Dec	Helios Fairfax (Africa)	Exchange					$62 million realized loss; Fairfax Africa put out of its misery
Dec	Easton (part of Peak)	Merger			$65		Rawlings (#1 baseball brand) for $65 million + 28% of Rawlings (in Peak?)
31-Aug	Sporting Life & Golf Town	Update					Fairfax owns 71% (up from 65.1%). Invested $74 mill total for current stake.
	Fairfax #1	Total return swaps					Market value = US$484.9 = 1.4 mill shares of FFH @ US$344.45/C$443.93
	Torstar	Sell					$52 million realized loss
	BDT Capital Partners	Sell down position?					$182 million realized gain
	Stocks (Exxon, Can Banks, Shell, GOOG, Fed Ex)				$212		$212 million realized gain = 40% avg investment
	Corporate Bonds	Buy		$3,900			Yield 4.1% and term of 4 years
	Equity hedges					$529	Final position sold. 11 year tragedy / catastrophe ended.
	CPI-linked derivative contracts						
		Total 2020	$600	$6,206	$849	$1,018	

			Insurance		Non-Insurance		
			Sale	Buy	Sale	Purchase	Average exchange rate CAN$ to US$ $0.7978
Date	**2021**	All figures are US$	**Proceeds**	**Cost**	**Proceeds**	**Cost**	**Comments**
Jan	Pet Health	Folded into Crum					
Jan	Ki #3	Begins writing business					
March	Farmers Edge	IPO					IPO raised $144 million. Over the years Fairfax invested C$376 million.
March	Boat Rocker	IPO					IPO raised $170 million. Fairfax has invested to date $110 million.
02-Mar	Ambridge Partners	Merges US MGA (Brit Global Specialty USA with Ambridge)					Brit owns 100% of Ambridge: manage + $450 mill in premium in US, and +
11-Mar	Churchill Manitoba port railway	Fairfax exits participation					Along with AGT
31-Mar	Helios Fairfax Partners	Debentures & warrants				$100	3% debs & warrants to buy 3 mill HFP shares ex at $4.90 (5 yr timeframe)
Q1	Rouge Media	Exit position			$10		
Q1	Fairfax #2	Total return swaps					Original notional amount = US$732.5 = 1.964 mill shares of FFH @ US$372
Q1	Thomas Cook	Preferred Shares				$60	Fairfax holds 248.2 mn shares. Preferred shares have conversion provision
April	Atlas #6	Grant of warrants					Fairfax granted 5 million warrants ex at $13; final part of APR deal?
14-Jun	Atlas #7	Redeem Debt			$600		5.5%; secured
		Debt buy				$300	5.5%; unsecured
		Preferred share buy				$300	7% dividend first 5 years; with 1.5% increases annually thereafter
		Grant of warrants					Fairfax also gets 1 million warrants exercise price @ $13.71/share
17-Jun	Singapore Re	Re-insurance buy		$103			Increased ownership from 28.1% to 96%; afterwards increased to 100%
05-Jul	Digit #2	Fund raising round					Fairfax booked $1.4 billion unrealized gain. $200 million raised by Digit fro
14-Jul	Eurolife #3	Life insurance buy		$143			Acquired 30% stake from OMERS; Fairfax owns 80% Eurobank owns 20%
05-Aug	Mosaic Capital	Take private - Mark Yusishen					Fairfax owns $131 million in 25 year debentures = 20% equity interest in n
06-Aug	Foran Mining	New equity buy				$78	55.5 million shares @ C$1.80/share
		Warrants					8 million warrants @ C$2.09/share
09-Aug	Quess	Sell down position			$36		Fairfax sold 3 million shares; still owns 30%
19-Aug	Toys "R" Us Retail	Retail operations sale			$90		Fairfax still owns real estate
23-Aug	Riverstone Europe (Runoff)	Insurance sale	$696				Sold 60% to CVC Capital Partners
			$236				Contingent value instrument; entitled to be reeived post-closing
							Asset Value Loan Notes - $1.3 billion of investments sold to CVC ($1.1 billi
27-Aug	Brit Insurance	Sale of 14% interest	$375				OMERS
07-Sep	Gulf Insurance Group	Insurance buy					For $475 million purchased AXA's ops in MENA
30-Sep	Mastercraft	Exit position			$49		Q3 13F; 1.868 million shares X $26 estimated value
30-Sep	Lumen Technologies	Exit position			$18		Q3 13F; 1.425 million shares X $12.50 estimated value
30-Sep	H&R Block	New equity buy				$28	Q3 13F; 1.12 million shares X $25 estimated value
11-Oct	Eurobank	Mexico transaction					Eurobank's impaired loan ratio falls to 14% from 29%. €3.2 billion sold to c
17-Nov	Odyssey Re	Sale of 9.9% interest	$900				CCIB & OMERS
Dec	Fairfax share repurchase					$1,000	2 million shares @ $500/share
10-Dec	IIFL Finance	Sell down position			$114		Fairfax sold 7% stake held directly; still hold via Fairfax India
16-Dec	IIFL Wealth	Sell down position			$78		Fairfax sold 4.27% stake held directly; Fairfax India sold stake March 2022
Dec	Leon's Furniture	Exit position			$140		Fairfax tendered their 7.2 million shares C$25
Dec	Eurobank	Mexico transaction					Eurobank's impaired loan ratio falls to 7.3% from 15.6%. €3.2 billion sold t
	Corporate Bonds				$253		Sold $5.2bn in corp bonds acquired in March/April 2020 at yield of 1%; gair
		Total 2021	**$2,207**	**$246**	**$1,387**	**$1,866**	

			Insurance		Non-Insurance		
			Sale	Buy	Sale	Purchase	Average exchange rate CAN$ to US$ $0.7684
Date	**2022**	All figures are US$	**Proceeds**	**Cost**	**Proceeds**	**Cost**	**Comments**
16-Feb	Fairfax India #4	Add to position				$65	5.4 million shares @ $12/share; Fairfax owns 41.8% of Fairfax India
17-Feb	Avante Logixx Inc	Deb conversion				$6	Converted debentures to 5.3 million shares @ C$1.56/share = 19.9% owne
23-Feb	Kennedy Wilson	Preferred equity				$300	Perpetual preferred stock with 4.75% annual dividend
		7 year Warrants					13 million common shares; $23 strike price
	First mortgage debt investment platform						$3 billion added; total platform = $5 billion
25-Mar	Farmers Edge	Loan				$75	Loan from Fairfax
30-Mar	Atlas #8	Exercise of warrants				$201	25 mill shares @ $8.05; Fairfax owns 45.1% (124.8 million shares)
							Fairfax still owns 6 million warrants
14-Apr	Altius	Exercised warrants				$78	Exercised 6.67 million warrants @ C$15 = 13.94% ownership
26-Apr	Ensign Energy Services	Deb conversion				$9	Fairfax owns 12.87%. Converted debs to 6.3 mill shares @ C$1.75/share.
01-Jun	S&P Global Ratings	Upgrade Fairfax Subsidiaries					core ins and reins subsidiaries to “A” from “A-” with a stable outlook.
		Upgrade Fairfax holding company					raised its long-term issuer credit rating on the holding company to “BBB” f
20-Jun	Pet insurance sale to JAB	Insurance sale	$1,400				$1,278 million pre-tax gain; $992 million gain after tax.
	JAB notes	Seller debentures				$250	
	JAB - JCP V investment fund	New equity buy				$200	
22-Jun	John Keells Holdings	Convertible Debentures				$75	208 million debentures (convert at Rs130); 3% interest rate; would bump F
30-Jun	Bank of America	New equity buy				$96	Q2&Q3 13F; 2.569 million shares to 3.1 million
30-Jun	Occidental Petroleum	New equity buy				$54	Q2&Q3 13F; 886.5 to 921 thousand shares
30-Jun	Chevron	New equity buy				$45	Q2 13F; 314 thousand shares (1/2 bought in Q2 & 1/2 bought Q3 2021)
30-Jun	BABA	New equity buy				$33	Q2 13F; 292.8 thousand shares (1/2 bought in Q2)
	Thomas Cook	Conversion preferred shares					Fairfax owns 6.6% more; during 1H 2022. Owns 73% (340.3mn), up from 6
	Farmers Edge	Write down				$109	
05-Jul	Resolute FP sale	Exit position			$626		Paper Excellence US$2.7 billion buyout; 30.548 shares x $20.50; Q1 2023 cl
	On close $665.6 ($44.2 CVR)	Contingent Value Right			$183		CVR of up to $6/share future duty deposit refund x 30.548 million shares
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04-Aug	Atlas take private				$0	$0	US$14.45/share; no new cash from Fairfax
09-Aug	Recipe	Take private				$342	FFH stake increased from 46 to 84%; Phelan family 16%. Paid C$20.73/sha
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		Upgrade Fairfax holding company					raised its long-term issuer credit rating on the holding company to “BBB” f
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09-Aug	Recipe	Take private				$342	FFH stake increased from 46 to 84%; Phelan family 16%. Paid C$20.73/sha
11-Aug	Western P&C Insurance Co	Insurance buy					Buyer was RiverStone US; run-off specialist of Fairfax; size of co and purch
11-Aug	Fairfax	Debt issuance	$750				Interest rate: 5.625%; to buy Allied World minority stake
27-Sep	Allied World	Add to position		$733			FFH own incr. 70.9% to 82.9%; recorded loss of $228 mill in retained earnir

11-Aug	Fairfax	Debt issuance	$750				Interest rate: 5.625%; to buy Allied World minority stake
27-Sep	Allied World	Add to position		$733			FFH own incr. 70.9% to 82.9%; recorded loss of $228 mill in retained earnin
30-Sep	Micron Technologies	Add to position				$152	Increased position from 693,000 to 3.462 million
24-Oct	Foran Mining	Exercised warrants				$25	16 million at C$2.09; owns 27.9% of Foran (27.8+43.8 = 71.6 million shares
12-Dec	Duke Royalty Ltd (UK)						New GBP100 million credit facility agreement - SONIA +5% (replace existi
							Includes 41.6 million warrants with 5 yr maturity strike of 45 pence
13-Dec	Mytilineos	Add to position				$53	Fairfax now owns 4.68%; 2.7 mill shares @ €18.5 = €50 million.
		Exchangeable Bond					option for 2.5 million shares @ €20 = €50 million (to Dec 2024)
14-Dec	Chorus Aviation	Debenture redemption			$85		Debentures (C$115 million) were redeemed at par; expected Dec 30 close.
		Warrants Expiration					Warrants (C$8.25 exercise price) expired upon redemption.
Q4	Sprting Life Group Limited	Add to position					Increased ownership from 71% to 88.5% in Q4. Funded via retained earning
		Total 2022	**$2,150**	**$733**	**$894**	**$2,363**	

			Insurance		Non-Insurance		
			Sale	Buy	Sale	Purchase	
Date	**2023**	All figures are US$	**Proceeds**	**Cost**	**Proceeds**	**Cost**	**Comments**
01-Jan	IFRS 17 - Account Change - All insurers in Canada						Increased common shareholders' equity by $2.4 billion and BVPS by $104.6
09-Jan	Ambridge Partners / Brit #3	Sale	$379				Sold to Amynta Group; $259.1 million pre-tax gain; $265.8 cash + $113.2 m
	Final deal details (differn't than anı	Performance target	$100				Receivable based on 2023 perofmance targets of Ambridge.
13-Jan	Atlas #9	Exercised Warrants				$65	5 million @ $13
		Exercised Warrants				$14	1 mill @ $13.71; FFh owns 130.8 mill shares (45.5%) of Atlas at Jan 13, 23
10-Feb	Mytilineos	Convertible bond				$53	Option 2.5 mill shares @ €20 = €50 mill. Will boost FFH stake to 6.43%
21-Mar	Antenna Plus (Greece)	Initial investment for 15% stake					Amount unknown. Streaming service. Private holding (Anennna Group)
29-Mar	Quess	Add to position					6.6 million shares; Fairfax owns 34.06% of Quess
Q1	Occidental Petroleum	Add to position				$130	Q1 added 2.1 millon shares; own 3 million
Q1	Micron	Add to position				$23	Q1 added 377 thousand shares; own 3.8 million
Q1	Orla Mining	Add to position				$21	Q1 added 4.6 million shares; own 15.4 million
Q1	Bank of America	Add to position				$9	Q1 added 301 thousand; own 3.4 million
19-Apr	Gulf Insurance Group	Buy out Kipco		$860			Buy Kipco stake = 46%; Fairfax will own 90% at close later this year.
	Fair value consideration = $740 ($200-$23+$563 fair value of payment deed)						$200 mill at close + 4 annual payments = $165 mill (start one year after cl
	Pre-tax gain = $290	Dividend	$23				Dividend paid by GIG to Kipco in Q2-2023.
05-Jun	Kennedy Wilson	PacWest real estate loans				$1,800	future funding +$1.7 billion? Avg ann return on capital deployed = 10%.
							avg term to maturity = 1.7 years (some extensions); LTV = 51%; 70% housi
05-Jun	Kennedy Wilson	Preferred Stock				$200	6% dividend
		Warrants					12.3 million common shares ex at $16.21; 7 year
26-Jun	Hostelworld Group (UK) - HSW.L	Increase in position					owns 5.25% of voting shares (up from 4.11%) = 6.49 million shares?
Q2	Poseidon / Altas #10	Increase in position				$11	Prem sold 678,021 shares to FFH at $15.50/share
Q2	Allied World	Increase in position		$30.6			Increased ownership from 82.9 to 83.4%
							Extended option to take out minority shareholders from Sept 24 to Sept 26
Q2	Occidental Petroleum	Add to position				$177	Position increased to 6 million shares from 3 million.
Q2	Orla Mining	Add to position				$25	Position increased to 19.9 million shares from 15.4 million.
Q2	Vanguard Index - S&P500 (VOO)	New Position				$34	
Q2	Bank of America	Exit position			$100		100% of position sold in Q2
Q2	Chevron	Exit Position			$50		100% of position sold in Q3
Q2	General Electric	Reduce Position			$8		Position reduced to 98.9 million shares from 173.9 million.
1H	Global Insurers and Reinsurers	Dividend payment		$136			1H-2023 payment to non-controlling interests. Last year was $177.7
	Run-off	Adverse development 1H		$80			
17-Aug	IIFL Securities	Reduce Position			$12		Ownership reduced from 9.28% to 3.38%. Shares sold for avg 65.55 rupee.
22-Aug	Meadow Foods	New Position					£550 million in sales; Fairfax has majority position. Year to March 2022, ge
20-Sep	Ovostar Union PCL	Add to position				$8	Added 10.01% for PLN 31.2 million for PLN 52 / share; Owns 27.51%.
Q3	Orla Mining	Add to position				$33	Position increased to 31.1 million shares from 19.9 million.
13-Nov	Blackberry #5	Debenture redemption			$365		1.75%; convertible at $6 to shares (55 milion)
		Debenture Extension to Feb 14, 2024				$150	1.75%; convertible at $6 to shares (25 milion)
17-Nov	Farmers Edge	Take Private					C$0.25/share (IPO was $17/share)
29-Nov	Thomas Cook India	Reduce Position			$67		Sold 40mn shares at INR 139.50 = INR 5.58bn. Still holds 300.2 mn shares.
06-Dec	Kennedy Wilson	Debt Platform					With KW, Fairfax increases commitment by $2 billion from $8bn to $10bn.
07-Dec	Fairfax	Debt Offering					US$400 million at 6% (upsized to $600 million in January)
11-Dec	Orla Mining	Add to position				$7	Added 2.5mn shares at C$3.82/sh. Owns 33.6 mn or 10.7% of shares outst
12-Dec	Foran Mining	Capital raise				$7	Added 2.439 million shares at C$4.10; new total = 73.995 million shares =
Q4	Intel	Reduce Position			$28		Share count reduced from 752.5k to 190k @ $50/share?
Q4	General Electric	Reduce Position			$9		Share count reduced from 93.3 to 25.6 @ $128/share?
Q4	Google	Reduce Position			$8		Share count reduced from 334.6 to 274.6 @ $139.7/share?
Q4	Orla Mining	Add to position				$21	Share count increased from 31.1 to 37.6mn @ US$3.23
11-Feb	Brian Young	From Odyssey to Fairfax					share oversight responsibilities with Andy Barnard, President of Fairfax Ins
		Total 2023	**$502**	**$1,107**	**$647**	**$2,788**	

			Insurance		Non-Insurance		
			Sale	Buy	Sale	Purchase	
Date	**2024**	All figures are US$	**Proceeds**	**Cost**	**Proceeds**	**Cost**	**Comments**
03-Jan	Fairfax	Annual Dividend					US$15/share (50% increase)
12-Jan	Fairfax	Debt Offering					Additional US$200 million at 6% (Dec 23 issued $400 million).
29-Jan	Fairfax	Debt Early Redemption					US$279 million at 4.875% (was due Aug 13, 2024)
31-Jan	Orla Mining	Add to position (couple of adds in Jan)				$61	Added 17.7 million shares in Jan/Feb at est cost of C$4.6/share
08-Feb	Blackberry #6	Debenture redemption			$150		Fairfax exits Blackbery debs. Prem also resigned from Blackberry board.
Q1	Intel	Reduce Position					
01-Mar	John Keells	Add to position				$46	Owns 19.4%; Converted 110 million debentures at 130/share. 98.1 million
		Total 2024	**$0**	**$0**	**$150**	**$107**	