

FAIRFAX FINANCIAL HOLDINGS

Interim Report for the six months ended June 30, 1998

To Our Shareholders:

In the second quarter net earnings decreased 8% to \$58.1 million from \$62.9 million last year. Net earnings per share for the second quarter decreased to \$4.79 per share from \$6.01 per share last year. The weighted average outstanding shares in the second quarter were 12.1 million versus 10.5 million last year.

Revenue in the second quarter increased to \$648.2 million from \$545.2 million as a result of increased premium, interest and dividend income, mainly related to the December 3, 1997 acquisition of Sphere Drake Holdings Limited (now renamed Odyssey Reinsurance, London and Bermuda).

The combined ratio in the second quarter increased to 108% from 106% last year due to recent acquisitions and greater pricing competition.

Interest and dividend income in the second quarter increased to \$87.5 million from \$52.4 million last year. Realized gains on disposal of portfolio securities were \$51.0 million in the second quarter compared to \$64.7 million last year. At June 30, 1998 the Fairfax investment portfolio had a pre-tax unrealized gain of \$61.3 million compared to an unrealized gain of \$122.7 million at December 31, 1997.

The previously announced acquisitions of Crum & Forster Holdings, Inc. and two Skandia reinsurance companies are expected to close during the third quarter, and the earnings from these companies to be acquired are therefore not included in the 1998 second quarter earnings of Fairfax.

During the second quarter Lindsey Morden Group Inc. completed the acquisition of Hambro Insurance Services for about \$217 million. Lindsey Morden financed the acquisition with an \$80 million equity issue (of which Fairfax took its 64.5% share) and a \$125 million 7% 10 year unsecured debenture issue. The increase in goodwill as at June 30, 1998 is due to the Hambro acquisition by Lindsey Morden.

During the quarter, Fairfax increased its unused, unsecured, committed long term bank lines to over \$1.3 billion.

Shareholders' equity at June 30, 1998 was \$1.96 billion or about \$161 per share.

August 4, 1998



V. PREM WATSA
Chairman and Chief Executive Officer

FAIRFAX FINANCIAL HOLDINGS

Interim Report for the six months ended June 30, 1998

CONSOLIDATED BALANCE SHEETS

as at June 30, 1998 and December 31, 1997

(unaudited - \$ millions)

	<u>1998</u>	
<u>1997</u>		
ASSETS		
Cash and short term investments	1,133.2	
207.1		
Accounts receivable	1,863.1	
1,669.8		
Recoverable from reinsurers	2,224.6	
2,164.5		
Claims in process	31.9	
14.9		
Income taxes refundable	25.8	
31.5		
Prepaid expenses	18.6	
<u>21.8</u>	<u>5,297.2</u>	
<u>4,109.6</u>		
<i>Portfolio Investments</i>		
Cash and short term investments	686.0	
823.8		
Bonds -		
(market value - \$4,138.6; 1997 - \$3,970.2)	3,987.3	
3,853.5		
Preferred stocks -		
(market value - \$321.2; 1997 - \$297.1)	301.7	
271.6		
Common stocks -		
(market value - \$622.1; 1997 - \$588.1)	731.6	
585.1		
Real estate	63.5	
<u>54.6</u>		
Total (market value - \$5,831.4;		
1997 - \$5,711.3)	<u>5,770.1</u>	
<u>5,588.6</u>		
Deferred premium acquisition costs	207.9	
220.1		
Deferred income taxes	167.8	
169.5		
Capital assets	80.3	
54.4		
Goodwill	170.4	
41.3		

Other assets	<u>46.6</u>	—
<u>23.8</u>		
	<u>11,740.3</u>	
<u>10,207.3</u>	-----	

LIABILITIES		
Bank indebtedness	35.3	
0.6		
Accounts payable and accrued liabilities	297.7	
282.5		
Premium deposits	<u>111.8</u>	—
<u>105.7</u>		
	<u>444.8</u>	—
<u>388.8</u>		
Provision for claims	6,506.5	
6,322.7		
Unearned premiums	1,130.7	
1,113.9		
Contingent value rights	23.2	
46.0		
Long term debt	<u>1,439.7</u>	—
<u>735.6</u>		
	<u>9,110.1</u>	
<u>8,218.2</u>		
Non-controlling interest	<u>50.1</u>	—
<u>20.5</u>		
SHAREHOLDERS' EQUITY		
Capital stock	1,222.3	
766.7		
Retained earnings	<u>739.9</u>	—
<u>629.0</u>		
	<u>1,962.2</u>	
<u>1,395.7</u>		
	<u>11,740.3</u>	
<u>10,207.3</u>	-----	

FAIRFAX FINANCIAL HOLDINGS

Interim Report for the six months ended June 30, 1998

CONSOLIDATED STATEMENTS OF EARNINGS

for the six months ended June 30, 1998 and 1997

(unaudited - \$ millions, except per share data)

<u>six months</u>		<u>Second quarter</u>		<u>First</u>
<u>1998</u>	<u>1997</u>	<u>1998</u>	<u>1997</u>	<u>—</u>
Revenue				
Gross Premiums written		584.3	516.4	
1,285.0	954.4			
Net Premiums written		475.2	396.8	
903.8	740.3			
Premiums earned		464.9	386.9	
927.2	755.5			
Claims fees		44.8	41.2	
87.4	79.5			
Interest and dividends		87.5	52.4	
163.9	113.0			
Realized gains on investments		51.0	64.7	—
106.9	82.1			
		<u>648.2</u>	<u>545.2</u>	
<u>1,285.4</u>	<u>1,030.1</u>			
Expenses				
Losses on claims		335.9	283.9	
680.1	561.4			
Operating expenses		130.2	98.1	
249.4	213.1			
Interest expense		20.3	10.9	
34.2	20.4			
Commissions, net		85.4	63.6	—
177.8	109.9			
		<u>571.8</u>	<u>456.5</u>	
<u>1,141.4</u>	<u>904.8</u>			
Earnings before income taxes				
		76.4	88.7	
144.0	125.3			
Provision for income taxes		18.1	25.7	—
32.6	30.3			
Earnings from operations				
		58.3	63.0	
111.4	95.0			

Non-controlling interest	<u>(0.2)</u>	<u>(0.1)</u>	<u>—</u>
<u>(0.5)</u> <u>(0.2)</u>			
Net earnings	<u>58.1</u>	<u>62.9</u>	<u>—</u>
<u>110.9</u> <u>94.8</u>	<u>-----</u>	<u>-----</u>	

Net earnings per share	\$4.79	\$6.01	
\$9.54 \$9.06			
Shares outstanding (000)	12,132	10,466	
11,618 10,466			
(weighted average)			

FAIRFAX FINANCIAL HOLDINGS

Interim Report for the six months ended June 30, 1998

CONSOLIDATED STATEMENTS OF RETAINED EARNINGS
for the six months ended June 30, 1998 and 1997
(unaudited - \$ millions)

	<u>1998</u>	—
<u>1997</u>		
Retained earnings - beginning of period	629.0	
397.7		
Net earnings for the period	110.9	
94.8		
Excess over stated value of shares purchased for cancellation	<u>--</u>	—
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Retained earnings - end of period	<u>739.9</u>	
<u>492.5</u>		

FAIRFAX FINANCIAL HOLDINGS

Interim Report for the six months ended June 30, 1998

CONSOLIDATED STATEMENTS OF CHANGES IN CASH RESOURCES
for the six months ended June 30, 1998 and 1997
(unaudited - \$ millions)

	<u>1998</u>	<u>1997</u>
Operating Activities		
Earnings from operations	111.4	95.0
Amortization	6.5	6.1
Deferred income taxes	8.1	1.0
Gains on investments	<u>(106.9)</u>	<u>(82.1)</u>
	19.1	20.0
Increase (decrease) in provision for claims	183.8	(20.7)
Increase (decrease) in unearned premiums	16.8	(16.6)
Decrease in cash funds resulting from changes in other operating working capital items	<u>(50.6)</u>	<u>(5.0)</u>
Cash resources provided by (used in) operating activities	<u>(169.1)</u>	<u>(22.3)</u>
Investing Activities		
Investments - purchases	(353.2)	(113.2)
Purchase of capital assets	(28.4)	(4.6)
Purchase of subsidiary, net of cash acquired	<u>(223.0)</u>	<u>(63.6)</u>
	<u>(604.6)</u>	<u>(54.2)</u>
Financing Activities		
Net capital stock transactions	455.6	--
Increase in long term debt	704.1	51.5
Change in non-controlling interest	<u>29.4</u>	<u>(1.5)</u>
	<u>1,189.1</u>	<u>50.0</u>
Decrease in cash resources	753.6	(26.5)
Cash resources - beginning of period	<u>1,030.3</u>	<u>611.9</u>
Cash resources - end of period	<u><u>1,783.9</u></u>	<u><u>585.4</u></u>

Cash resources consist of cash and short term investments less bank indebtedness and short term borrowings.

FAIRFAX FINANCIAL HOLDINGS

Interim Report for the six months ended June 30, 1998

SOURCES OF NET EARNINGS
(Lindsey Morden equity accounted)
for the six months ended June 30, 1998 and 1997
(unaudited - \$ millions)

	<u>1998</u>	<u>1997</u>
Insurance underwriting	(70.0)	(45.2)
Interest and dividends	<u>144.9</u>	<u>110.1</u>
	74.9	64.9
Claims adjusting (Fairfax portion)	0.9	0.4
Interest expense	(33.4)	(19.4)
Goodwill amortization	(2.5)	(2.4)
Corporate overhead and other	(5.0)	(1.1)
Realized gains on investments	<u>106.9</u>	<u>82.1</u>
Pre-tax income	<u>141.8</u>	124.5
Less: taxes (recovery)	<u>31.1</u>	<u>29.7</u>
Net earnings	<u><u>110.9</u></u>	<u><u>94.8</u></u>
Combined ratio	<u>108%</u>	<u>106%</u>

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CAPITAL STRUCTURE
(Lindsey Morden equity accounted)
as at June 30, 1998 and December 31, 1997
(unaudited - \$ millions, except per share data)

	<u>1998</u>	—
<u>1997</u>		
Cash and short term investments	1,133.2	
207.1		
Long term debt	1,295.8	
718.4		
Net debt	162.1	
511.3		
Common shareholders' equity	1,962.2	
1,395.7		
Net debt/equity	8%	
37%		
Net debt/capital	8%	
27%		
Shareholders' equity per share	161.7	
125.4		

Parent company cash and short term investments includes approximately US\$680 million of short term investments available for the purchase of Crum & Forster.