FAIRFAX
FINANCIAL HOLDINGS LIMITED

1992 Annual Report

F A I R F A X
L O G O

1992 Annual Report

Contents

FAIRFAX

FINANCIAL HOLDINGS LIMITED

Eight Year Financial Highlights

(in thousands except per share data)

			1992	1991	1990	1989	1988	1987	1986	1985
Total revenue	286,830		250,002	195,430	125,754	133,649	112,971	53,733	17,015	
Net earnings	10,045		22,515	21,306	16,741	14,357	16,019	6,548	(910)	
Total assets	590,548		516,564	535,987	248,065	246,786	185,413	129,845	41,477	
Shareholders' equity	143,818		116,775	94,676	90,830	74,176	61,048	41,275	10,379	
Shares outstanding	year-end		6,055	5,455	5,477	7,316	7,322	7,337	7,007	5,000
Return on average equity	7.7%		21.3%	23.0%	20.3%	21.2%	31.3%	25.4%		
Per share										
	Net earnings	fully diluted	1.76	3.94	2.92	2.25	1.94	2.23	1.35	(1.89)
	Shareholders' equity		23.76	21.41	17.29	12.41	10.13	8.32	5.89	2.08
Market prices per share										
	High		30.00	22.50	21.63	19.00	15.13	17.50	14.13	6.00
	Low		21.75	10.75	8.88	14.00	11.75	10.50	6.00	3.00
	Close		25.00	21.25	11.00	18.75	15.00	12.37	12.75	6.00

Corporate Chart goes on this page

CORPORATE PROFILE

Fairfax Financial Holdings Limited is a financial services holding company whose corporate objective is to achieve a high rate of return on invested capital and build long term shareholder value. The company has been under present management since September 1985.

Commonwealth Insurance, based in Vancouver, was acquired in November 1990. It offers commercial property and oil and gas insurance in Canada, the United States and internationally, and commercial casualty insurance in Canada. In 1992 Commonwealth's gross premiums written totalled $161.3 million. Commonwealth has been in business since 1947 and at year-end there were 123 employees.

Federated was acquired in January 1990, and is based in Winnipeg. Its two companies market a broad range of insurance products primarily for commercial customers. In 1992 Federated's gross premiums written totalled $43.2 million, consisting of $34.5 million of property and casualty business and $8.7 million of life and group health and disability products. Federated has been in business since 1920 and at the end of 1992 had 227 employees.

Markel Insurance is one of the largest trucking insurance companies in Canada and has provided the Canadian trucking industry with a continuous market for this class of insurance since 1951. The company also insures small amounts of property and casualty risks and continues to run off its former reinsurance business. In 1992 gross premiums written were $47 million and the group had 73 employees.

Wentworth Insurance Company was incorporated in 1990 as a captive insurance company domiciled in Barbados. The company had total assets of $8.3 million at year-end.

Morden & Helwig Group Inc., acquired in 1986, is engaged in providing claims adjusting, appraisal and loss management services to a wide variety of insurance companies and self-insured organizations across Canada, the U.S. and the U.K. In 1992 revenue totalled $139.3 million. The company was established in 1923, and at year-end the group had some 1,700 employees located in 334 offices.

Hamblin Watsa Investment Counsel Ltd., acquired in 1992, provides discretionary investment management, primarily to pension funds and insurance companies, including the insurance company subsidiaries of Fairfax. Hamblin Watsa was founded in 1984 and at year-end managed approximately $1 billion with 11 employees.

To Our Shareholders

The inevitable happened. For the first time since we began in 1985, we did not earn a return on shareholders' equity in excess of 20%. We earned 7.7% on shareholders' equity in 1992 (vs 1.8% for the TSE 300). Net income after taxes in 1992 was $10 million or $1.76 per share, a 56% decrease from the $22.5 million or $3.94 per share reported in 1991. Book value per share, however, increased by 11% to $23.76 per share.

While these results were disappointing, over the last seven years Fairfax has earned an average annual return on shareholders' equity of 21.5% (vs 7.5% for the TSE 300), which is in excess of our objective of 20%. Book value has increased from $2.08 in 1985 to $23.76   a compound rate of about 40% that we do not expect to repeat.

A word about long term returns on shareholders' equity. In July of each year the Report on Business publishes a survey of the top 1,000 companies in Canada based on profits, revenue, assets and return on shareholders' equity. You may be surprised to know that in last year's issue, only 39 companies out of the top 1,000 earned in excess of 20% on equity over the previous five years. Fairfax was ranked 22nd last year. While the results to date have been gratifying, this shows that our 20% objective is not an easy hurdle. Nevertheless, we continue to have that as our objective over the next five years.

In 1992 we simplified our corporate relationships significantly by the purchase of Hamblin Watsa Investment Counsel Ltd. (HWIC) as well as a 49.9% interest in The Sixty Two Investment Company Limited (Sixty Two), the controlling shareholder of Fairfax. As I was a shareholder in both these companies and recognized the potential conflict of interest was very high, I want to make sure you understand how and why we did these transactions and why they were fair (I hope you agree!).

HWIC is an investment counselling firm that Tony Hamblin and I founded in 1984. With five partners, Tony Hamblin, Roger Lace, Brian Bradstreet, Frances Burke and me, who have worked together for 18 years, and Vito Maida, a recent addition, the firm manages approximately $1 billion in pension, corporate and individual funds. Of the $1 billion, approximately $240 million are funds that originate from Fairfax's insurance subsidiaries. From inception the firm was set up to manage a small number of portfolios with a long term value-oriented philosophy. All the clients agreed to an incentive fee, resulting in HWIC being more investment driven than marketing-oriented. The company's long term results have ranked among those of the top investment managers in Canada.

How did we value the firm? Firstly, we created an independent committee of our Board, chaired by Robbert Hartog. Secondly, we consulted Sir John Templeton, the dean of the investment counselling business and also a large shareholder of ours. After arriving at a price that both Robbert and Sir John felt was fair, we obtained written approval of this transaction from all of the more than 50% of our minority shareholders that we contacted. Thus, the valuation of $14 million ($1.85 million in cash and 433,773 Fairfax shares valued at $28 per share) was considered fair and approved by our Board of Directors, the majority of our minority shareholders and all the partners at HWIC.

Why did HWIC make sense for Fairfax? Mainly, for the following three reasons:

1) It was a very good investment for Fairfax. Under very reasonable assumptions (i.e. no incentive fees or additional funds under management), Fairfax could achieve its 20% return on investment. Also, a multiple of 3.8 times revenue and 8 times pre-tax earnings was reasonable compared to private transactions and public valuations of investment counselling firms. Furthermore, we paid for most of the purchase by issuing shares of Fairfax at a fair price of $28 per share.

2) It brought proven investment management into Fairfax.

3) It removed my perceived conflict of interest and placed all of my interests in one pot.

While we think HWIC will be an excellent investment for Fairfax, our purchase price, as Note 16 shows, was essentially all goodwill. We are amortizing this over 10 years even though we do not think there will be any decrease in goodwill over the years.

HWIC will continue to be run as a separate subsidiary with Tony Hamblin as President. We have maintained the incentives at HWIC by a fair structuring of revenue sharing. I welcome the partners and employees of HWIC to Fairfax and we look forward to some excellent long term returns from our investment.

The purchase of the 49.9% interest in Sixty Two was basically to provide liquidity to the original investors who backed me seven years ago, on terms attractive to Fairfax. Sixty Two's only asset is shares of Fairfax and it has no liabilities. The shares of Sixty Two were valued on the basis of the market price of the Fairfax shares owned by it, less a liquidity discount of 15%. As disclosed in Note 9, in essence Fairfax issued approximately 680,000 shares to acquire indirect ownership of about 800,000 of its shares. The net result was that Fairfax effectively repurchased approximately 120,000 of its shares (with a market value of over $3.3 million at $28 per share) for no cost. Book value and earnings per share will be about 2% higher because of this purchase. Sixty Two will continue to be controlled by me as it has been in the past. This purchase also was approved by our Board of Directors, the majority of our minority shareholders and all the investors in Sixty Two.

With the completion of these two transactions, Fairfax is much simplified in its relationships and perhaps more focused. Also, the purchase of the Sixty Two shares brings to an end (at least formally) the original partnership that refinanced Fairfax (then known as Markel Financial) in those early days in 1985. Looking back, these investors must have been special to have financed an almost bankrupt insurance holding company led by a chairman with no corporate experience at all. There may, after all, be some truth in the definition of an entrepreneur "Unreasonable conviction based on inadequate evidence"! Even though this group will continue to be shareholders for some time, I want to take this opportunity to thank them for their invaluable support, without which Fairfax would not have existed.

The table below shows the sources of our net earnings:

	($ millions)	
	1992	**1991**
Insurance underwriting	(16.9)	5.3
Interest and dividends	24.8	25.4
Total	7.9	30.7

Claims adjusting (Fairfax portion)	0.3	0.1
Investment banking and adjustments		(1.1)
Interest expense/corporate overhead	(4.8)	(6.5)
Realized gains	9.7	2.5
Income before taxes and provisions	13.1	25.7
Less: provisions for investment losses	(6.4)	(7.0)
Total pre-tax income	6.7	18.7
Less: taxes	(3.3)	9.8
Earnings after taxes	10.0	8.9
Gain on sale of F-M Acquisition	____	13.6
Net earnings	10.0	22.5

The table shows you the results from our insurance (underwriting and investments) and non-insurance operations. Shown separately are realized gains and provisions for potential losses so that you can better understand our earnings from our operating companies. Also, please note the unaudited statements of our combined insurance operations and Morden & Helwig's financial statements shown on pages **x** to **x**.

Insurance earnings declined significantly due to large underwriting losses which are discussed in greater detail later, and there was only an insignificant contribution from Morden & Helwig. In spite of higher realized gains and lower interest expense and corporate overhead, this resulted in pre-tax income before provisions declining by 50% to $13.1 million. After provisions and a recovery of past income taxes, we earned $10 million, up from $8.9 million last year. In 1991, however, we benefitted from a $13.6 million gain on the sale of our interest in F-M Acquisition Corporation which resulted in net earnings of $22.5 million. Our net earnings of $10 million are at their lowest level since 1986.

Insurance operations

We suggested last year that there were faint signs that the insurance cycle was turning and that the wind might be behind our back again. How wrong we were! Hurricane Andrew bore down on the industry with a vengeance and cost us approximately $11 million. Also, a few large losses, combined with wind storm damage at Otter Dorchester and a $1.5 million loss from the Laurentian Financial Services (LFS) program (including termination costs), resulted in Markel having an underwriting loss of $5 million. The combined underwriting loss in our insurance operations of almost $17 million was by far the largest loss we have had over the last five years (page **x]**). On a combined ratio basis, we came in at 114%, way above our target of 100%. That's the bad news. The good news is that in the main we could not have prevented these losses through better underwriting.

As suggested last year, Markel continues to focus on long haul trucking. By year-end Markel had disposed of its farm business in Otter Dorchester to the North Waterloo Mutual Insurance Company and cancelled its contract with LFS. Markel's business increased significantly in 1992 without any price discounting, partly because its largest competitor had financial problems. Markel had a combined ratio of about 115% excluding its discontinued lines. Bill Grant and his management team have consolidated Markel and focused it on long haul trucking. The trucking insurance business, however, continues to be very competitive.

Since we bought it in 1990, Federated Insurance, under John Paisley's leadership, has gone from a branch operation to an independent company with its own information systems. John and his management team continue to develop niche markets with a captive sales force. Federated's property-casualty and life insurance operations' combined ratio was 104% in 1992, and the company is poised for achieving consistent underwriting profitability.

Commonwealth, led by John Watson, had a difficult year in 1992 due to Hurricane Andrew which resulted in the company having a combined ratio of 122% its worst result in over five years. If not for Hurricane Andrew, Commonwealth's combined ratio would have been 98%. Unlike Hurricane Hugo ($2.7 million) and the Oakland earthquake ($1.4 million), Hurricane Andrew cost Commonwealth approximately $11 million, even though gross losses for Hugo were somewhat larger. Commonwealth continues to realize price increases in many of its insurance lines and, barring another major hurricane or earthquake, should contribute significantly to our earnings in 1993.

As mentioned in last year's annual report, there continue to be signs of a turn in the insurance underwriting cycle. We may have the wind behind our back again after having a headwind for five long years. While our insurance companies are writing more business than in 1991, our operating leverage (net premiums to common equity) continues to be only 0.9:1 for Markel, 1:1 for Federated and 0.6:1 for Commonwealth, versus a potential of at least 2:1. Thus when the cycle turns we, unlike many insurance companies, have the capacity to increase our premiums manyfold.

As you know, since we began in 1985, we have had The Wyatt Company certify our claims reserves by company and in total. How accurate have we been in our estimation of claims reserves? Have we been consistently over-reserved or under-reserved? To help you answer these and other questions, this year, for the first time, we have provided extensive disclosure on our total claims reserves in the section "Provision for claims" beginning on page **x**. While this disclosure is mandatory in the U.S., it is not a requirement in Canada. However, we feel that this information will help you better understand our insurance operations and we thus plan to disclose it annually. While there are no guarantees, we continue to feel that we are adequately reserved.

Claims adjusting

In spite of Hurricane Andrew, Morden & Helwig had a disappointing year in 1992. While net income increased to $562,000 from $234,000 in 1991, the results are still much below expectations. Ken Polley and his management team are working diligently to deal with the situations that arose from significant expansion in the U.S. while also coping with the poor claims environment in Canada. During 1992 Ken moved to the U.S., and we continue to be very confident that Morden & Helwig will return to significant profitability soon (to date I have been wrong!).

With the acquisition of the Renaud, Préfontaine group in Quebec, large capital expenditures for computerization and poor profitability, Morden & Helwig's long term debt increased in 1992. However, with a long term debt to common equity ratio of 0.4:1, Morden & Helwig continues to have a strong balance sheet although less strong than in the past.

Included in "Other assets" on the Morden & Helwig balance sheet on page **x** is goodwill amounting to $31.4 million as at December 31, 1992. This goodwill is consolidated into Fairfax's balance sheet. Most of this goodwill arose from the purchase of the original Lindsey & Newsom operations in Texas. As these operations continue to be very profitable and provide the base for the U.S. operations, we believe there is no diminution of goodwill. Also, even at its low of $6-$7 per share, Morden & Helwig sells at its book value per share of approximately $7.05, suggesting the goodwill is "good". We review the goodwill on Morden & Helwig's balance sheet on a regular basis and continue to feel comfortable that in a service business with 334 offices and 1,700 people, the goodwill is justified. There is nothing like improved profits, though, to make us (and you!) more comfortable.

Investment banking

This is the last time you will read this section in our reports and I'm sure you are very happy (I am!). We will be closing down our investment banking area. While not obvious in the table on page **x**, we had to make good on our guarantees at Carbovan for $5.75 million. We have used provisions from the past which have now proved to be unnecessary to offset the impact of this on our income statement. Including guarantees, our half of Carbovan has cost us $14 million since 1988 and we have nothing to show for it. You can be sure we will never get into a venture capital investment again. Unfortunately, it was a costly lesson we prefer to learn from the mistakes of others!

A management restructuring at Develcon resulted in our $1 million loan being settled for cash and Develcon shares. We have written down our Develcon shares to an insignificant amount even though we have not sold the shares. We first invested in Carbovan in 1988 and in Develcon in 1987. It took us between five and six long years to exit from these investments proving again that it is very easy to get into something but extremely difficult to get out. On a cumulative basis, your Chairman's brilliance has cost the company about $18 million or $3.00 per share pre-tax. On the positive side, this is history and will not affect us in the future. We continue to work at liquidating our real estate investments and expect to recover our costs (please see Note 2).

Financial position

As mentioned in previous annual reports, the best way to understand our financial position is to look at our unaudited balance sheet with Morden & Helwig equity accounted as shown on page **x**. Here is what it looks like compared to 1991:

($ millions)	**1992**	**1991**
Short and long term debt	47.7	30.8
Contingent debt Federated	20.4	20.4
Common shareholders' equity	143.8	124.3 *
Total capital	$211.9	$175.5

* Includes the convertible debenture that was converted into subordinate voting shares on February 14, 1992.

Our short and long term debt increased by approximately $17 million in 1992, mainly because we took almost no dividends from our insurance companies while financing the purchase of Hamblin Watsa ($1.85 million), the repurchase of about 109,000 Fairfax shares ($2.6 million), an investment in marketable securities at the Fairfax level ($5 million), Carbovan and other miscellaneous items.

Our shareholders' equity increased by $19.5 million because of net income of $10 million and net shares issued of $9.5 million ($12.1 million for Hamblin Watsa, less $2.6 million spent to retire 109,000 shares of Fairfax at an average price of $24 per share

(Note 9)).

Our short and long term debt position at year-end was higher than we expected for the reasons mentioned. In 1993 we plan to bring this debt down to about $30 million, at which point our debt level would be very comfortable in relation to our earnings and shareholders' equity base.

In 1992 we renegotiated our banking lines and raised them to $75 million, all on a revolving five year term basis. While these lines provide us with flexibility, we plan to always leave a significant portion of them undrawn.

As mentioned in last year's annual report, we have begun to finance our employee stock purchase loans at a bank (Note 4). During 1993 it is likely that almost all these loans will be financed independently in this manner. We are also looking at more efficient ways to make the key officers of Fairfax significant owners.

This is perhaps an appropriate time to discuss our share buyback philosophy. We believe that at stock prices close to book value, it benefits our shareholders if we buy back our shares and retire them, as long as this is done well within our financial capability. We do not find too many opportunities to invest at a 20% after tax rate of return assuming that is what we earn in the future. Many companies have share buyback plans but rarely use them. Here's what we have done since we began:

	1988	**1989**	**1990**	**1991**	**1992**	
Shares repurchased *(000s)*	14	6	1,839	21	109	(+120 *)
Average price *($)*	8	8	9	19	24	
Cost *($000s)*	112	48	17,460	399	2,616	

* 120,000 shares effectively retired for no cost due to the Sixty Two purchase.

On a cumulative basis, since we began we have retired approximately 2.1 million shares (including the Sixty Two purchase) at an average cost of $9.80 per share. This works out to approximately 34% of our current shares outstanding.

Given our planned reduction in debt levels in 1993, we continue to examine opportunities to expand in the insurance business. While we have examined many situations, nothing has come of them.

Investments

1992 was among the worst years we have experienced over the past 18 years managing Canadian stocks using a value-oriented philosophy. Stocks on the TSE that were among the cheapest on a value-oriented basis declined significantly in the second half of the year. On the other hand, our U.S. stock portfolios had an excellent year. However, we have more invested in Canada.

1991's year-end unrealized losses, which almost disappeared in the first quarter of 1992, increased again at year-end as shown below:

	($ millions)	
	1992	**1991**
Bonds	2.4	(0.3)
Preferred stocks	1.4	(0.8)
Common stocks	(21.2)	(5.0)
	(17.4)	(6.1)

The unrealized losses at the end of 1992 were after an aggregate provision for losses of $16.3 million, up from $9.9 million at the end of 1991 (please see Note 1). Thus if we had not increased our provision for losses in 1992, the unrealized loss at year-end would have been $6.4 million higher. What does all this mean? In the worst case, if we had to liquidate our portfolios as at December 31, 1992, our book value would be $17.4 million (or approximately $2.90 per share pre-tax) less than what we have shown it to be. We think this is pretty drastic but that is the downside.

The trend in our unrealized gains or losses as at December 31 is shown below:

1985	**1986**	**1987**	**1988**	**1989**	**1990**	**1991**	**1992**

Unrealized gains (losses)								
$ million	1.4	1.0	(6.9)	5.2	(1.1)	(34.0)	(6.1)	(17.4)
% of investment portfolio	4.3	1.1	(5.6)	3.8	(0.8)	(10.0)	(1.8)	(4.4)

My own view, as expressed often here in these pages, is that unrealized losses or gains are fluctuations and do not have any predictive value. At the end of 1990 we had an unrealized loss of $34 million which almost disappeared in early 1992. Realized gains or losses are what count over the long term. Having said that, we have provided $16.3 million for investment losses to take the possibility of permanent impairments into account. For example, with Woodward's having filed for protection from creditors, we have written off our total investment of $2 million even though we haven't sold it. Of the $16.3 million provision, approximately $5 million is specific, the rest being provisions against potential losses. We continue to feel that this provision is conservative, but only time will tell. Unrealized losses have dropped to $7.2 million as of March 17, 1993.

The table on page **x** shows the returns on the investment portfolio. As shown, realized gains after provisions have been below par in the past three years unlike the three years before that. We continue to believe that realized gains in the future will be significant even though we can't say when. I should note here that the TSE 300 is selling at only a 35% premium to book value while the S&P 400 sells at a 200% premium. Over the past 35 years, both markets have sold at comparable market to book value ratios. We expect this relationship to come back into balance as the TSE 300 outperforms the S&P 400.

Gross realized gains in 1992 totalled $11.8 million. After realized losses of $2.1 million and provisions of $6.4 million, net realized gains were $3.4 million. The major contributors to realized gains were Bank of Nova Scotia ($1.7 million), Magma Copper ($1.5 million), Nikkei puts ($1.4 million) and Old Republic ($0.9 million).

At the end of 1992 we had $33.4 million invested in the common shares of banks and insurance and financial service companies and $20.6 million in natural resource companies.

Finally, on pages **x** and **x**, you should note that over time the increase in our investment portfolio has resulted in a rising stream of dividend and interest income. The decrease in 1992 is a result of a shift towards high quality preferreds (dividends are more tax efficient). On an after tax basis, dividend and interest income continued to increase in 1992.

Please refer to our 1991 annual report for our press and/or investor relations policy. It is not long.

As discussed in our 1991 annual report, our donations policy is to donate annually at least 1% of our pre-tax income from operations to charities. Fairfax and its subsidiaries donated approximately $150,000 in 1992 to a variety of charities across the country.

I have always believed that the stock market fluctuates in the short term but always reflects economic reality in the long term. How about Fairfax? How has the market treated us? Since we began over seven years ago, Fairfax has sold below book value for only 1 years from March 1990 to September 1991 i.e. for approximately 20% of the time. The market has been pretty fair to us.

This also means that over time, every one dollar retained by Fairfax (as against paying it out in dividends) has resulted in at least one dollar of market value, with no taxes paid by our shareholders. As long as this test continues to hold (i.e. every dollar retained resulting in a dollar of increased market value) and we continue to earn 20% on our shareholders' equity, we won't be paying any dividends because it would be contrary to the interest of long term shareholders to whom we try to cater.

We continue to keep our holding company small. Brenda Adams, Sam Chan, Paul Fink, Rick Salsberg, Ronald Schokking and John Varnell continue to show what can be done with a small, exceptionally talented and hard working group of people.

So much for history! How about the future? It continues to be as uncertain and unpredictable as it always was. However, with good people and good fortune, we continue to labour towards our long term objective of earning in excess of 20% on shareholders' equity by running Fairfax and its subsidiaries for the long term benefit of customers, employees and shareholders.

On your behalf, I would like to thank the Board and the management and employees of all our companies for their very significant contributions throughout the challenges of 1992.

March 22, 1993

V. Prem Watsa

Chairman and

Chief Executive Officer

Fairfax Logo

CONSOLIDATED FINANCIAL STATEMENTS

For the years ended December 31, 1992 and 1991

Consolidated Balance Sheets

as at December 31, 1992 and 1991

	1992 *($000)*	**1991** *($000)*
Assets		
Cash and short term investments	83,495	72,362
Accounts receivable	99,369	95,983
Claims in process	12,391	12,523
Income taxes refundable	4,536	
Prepaid expenses	3,643	3,381
	203,434	184,249
Portfolio investments		
Bonds		
(market value $105,637; 1991 $114,086)	103,224	114,412
Preferred stocks		
(market value $108,597; 1991 $91,644)	107,160	92,482
Common stocks		
(market value $76,701; 1991 $56,934)	97,902	61,924
Total (market value $290,935; 1991 $262,664)	308,286	268,818
Other investments (note 2)	4,459	4,651
Deferred premium acquisition costs	6,307	6,128
Capital assets (note 3)	17,423	14,587
Goodwill (note 16)	42,701	23,995
Other assets (note 4)	7,938	14,136
	590,548	516,564

Signed on behalf of the Board

Watsa

Director

Hartog

Director

	1992 ($000)	1991 ($000)
Liabilities		
Bank indebtedness (note 5)	4,792	4,480
Short term borrowings (note 5)	1,532	5,807
Accounts payable and accrued liabilities	44,079	37,562
Future pension commitments	6,384	5,759
Premium deposits	5,844	3,993
Income taxes payable		2,476
	62,631	60,077
Provision for claims	208,816	202,120
Unearned premiums	66,135	55,044
Contingent long term debt (note 6)	20,445	20,445
Long term debt (note 7)	61,492	28,763
Deferred income taxes	9,810	8,866
	366,698	315,238
Non-controlling interest	17,401	16,974
Subordinated convertible debenture (note 8)		7,500
Shareholders' Equity		
Capital stock (note 9)	49,841	30,954
Retained earnings	93,977	85,821
	143,818	116,775
	590,548	516,564

Consolidated Statements of Earnings
for the years ended December 31, 1992 and 1991

	1992 ($000)	1991 ($000)
Revenue		
Premiums earned	118,854	90,507
Claims fees	139,782	122,982
Interest and dividends	23,988	26,051
Realized gains (losses) on investments	3,400	(4,512)
Other income	806	1,338
Gain on sale of associated company		13,636
	286,830	250,002
Expenses		
Losses on claims	90,868	54,267
Operating expenses	177,430	154,849
Interest expense	7,650	8,772
Commissions, net	3,907	(351)
	279,855	217,537
Earnings before income taxes	6,975	32,465
Provision for (recovery of) income taxes (note 11)	(3,352)	9,832
Earnings from operations	10,327	22,633
Non-controlling interest	(282)	(118)
Net earnings	10,045	22,515
Net earnings per share fully diluted (note 15)	$1.76	$3.94

Consolidated Statements of Retained Earnings
for the years ended December 31, 1992 and 1991

	1992 ($000)	1991 ($000)
Retained earnings beginning of year	85,821	63,556
Net earnings for the year	10,045	22,515
Excess over stated value of shares purchased for cancellation (note 9)	(1,889)	(250)
Retained earnings end of year	93,977	85,821

Consolidated Statements of Changes in Cash Resources

for the years ended December 31, 1992 and 1991

	1992 ($000)	1991 ($000)
Operating activities		
Earnings from operations	10,327	22,633
Amortization	5,301	3,784
Deferred income taxes	944	2,488
Losses (gains) on investments	(3,400)	4,512
	13,172	33,417
Increase (decrease) in provision for claims	6,696	(18,482)
Increase in unearned premiums	11,091	2,325
Decrease (increase) in cash funds resulting from changes in other operating working capital items	(1,536)	6,359
Cash resources provided by operating activities	29,423	23,619
Investing activities		
Portfolio investments net sales (purchases)	(36,068)	14,575
Sale (purchase) of capital assets	(6,760)	3,333
Investment in Hamblin Watsa Investment Counsel Ltd. (note 16)	(1,854)	
Other investments	129	7,165
	(44,553)	25,073
Financing activities		
Net capital stock transactions	4,852	(1)
Increase (decrease) in long term debt, net of debt conversion	25,229	(13,636)
Increase in non-controlling interest	145	153
	30,226	(13,484)
Increase in cash resources	15,096	35,208
Cash resources beginning of year	62,075	26,867
Cash resources end of year	77,171	62,075

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

Notes To Consolidated Financial Statements

for the years ended December 31, 1992 and 1991
(in $000s except per share amounts and as otherwise indicated)

1. Summary of Significant Accounting Policies

Business operations

The company is a financial services holding company which through its subsidiaries and affiliates is engaged in the insurance of commercial property, oil and gas, casualty and life risks and the provision of claims adjusting, appraisal and loss management services in Canada and the United States.

Principles of consolidation

The consolidated financial statements include the accounts of the company and all of its subsidiaries: Markel Insurance Company of Canada, Federated Insurance Holdings of Canada Ltd., Commonwealth Insurance Company, Wentworth Insurance Company Ltd. and Hamblin Watsa Investment Counsel Ltd., all 100% owned; and Morden & Helwig Group Inc., 50% equity and 90% voting interest. Acquisitions are accounted for by the purchase method, whereby the results of acquired companies are included only from the date of acquisition. Divestitures are included up to the date of disposal.

Premiums

Insurance premiums are taken into income evenly throughout the terms of the related policies. As premium deposits secure the payment of premiums and are refundable, they are not taken into income unless default in payment of premiums occurs.

Claims in process

The company records its inventory of claims in process at its estimated value at year-end, based on a determination of the claims in process at year-end through a complete physical count of related files. Claims adjustment fees arising therefrom are accounted for on an estimated percentage-of-completion basis.

Deferred premium acquisition costs

The costs incurred in acquiring insurance premiums are deferred, to the extent that they are considered recoverable, and amortized over the same period as the related premiums are taken into income.

Investments

Bonds are carried at amortized cost providing for the amortization of the discount or premium on a straight line basis to maturity. Preferred and common stocks are carried at cost. When there has been a loss in value of an investment that is other than temporary, the investment is written down to its estimated net realizable value.

The realized gains (losses) on investments recorded in the income statement are net of provisions for losses on investments of $6.4 million (1991 $7 million). At December 31, 1992 the aggregate provision for losses on investments was $16.3 million (1991 $9.9 million).

Investment income

Investment income is recorded as it accrues. Dividends are recorded as income on the record date. Gains and losses realized on the disposal of investments are taken into income on the date of disposal.

Provision for claims

Claim provisions are established by the case method as claims are reported. The provisions are subsequently adjusted as additional information on the estimated amount of a claim becomes known during the course of its settlement. A provision is also made for management's calculation of factors affecting the future development of claims including claims incurred but not reported based on the volume of business currently in force and the historical experience on claims.

Translation of foreign currencies

Assets and liabilities in foreign currencies are translated into Canadian dollars at year-end exchange rates. Income and expenses are translated at the exchange rates in effect at the date incurred. Realized gains and losses on foreign exchange are recognized in the statements of earnings.

Goodwill

The difference between purchase cost and the fair value of the net assets of acquired businesses is amortized on a straight line basis over its estimated useful life which ranges from 10 to 40 years. The goodwill is primarily related to the company's investments in Morden & Helwig Group Inc. and Hamblin Watsa Investment Counsel Ltd.

2. Other Investments

	1992	**1991**
	($000)	*($000)*
Real estate	4,459	4,651

The company has invested in several small real estate projects in Alberta, Texas and Ontario, the major one being a 100% interest in a shopping mall in Calgary, Alberta. This investment of $2.3 million (1991 $2.2 million) is shown net of a 12.04% mortgage of $4.9 million (1991 $5 million), due June 1994, which is non-recourse to Fairfax Financial Holdings Limited and for which the shopping mall has been pledged as security.

3. Capital Assets

	1992	**1991**
	($000)	*($000)*
Land and buildings	4,104	4,147
Furniture and equipment	25,630	22,742
Leasehold improvements	1,467	1,378
Automobiles under capital lease	527	412
	31,728	28,679
Accumulated amortization	14,305	14,092
	17,423	14,587

4. Other Assets

Included in other assets are non-interest bearing loans to officers and directors of the company and its subsidiaries under the company's employee stock purchase plan totalling $4,196 (1991 $9,260) for which 275,373 shares (1991 649,573 shares) with a year-end market value of $6,884 (1991 $13,803) have been pledged as security. The company may under certain circumstances be obligated to purchase loans to officers and directors of the company and its subsidiaries from a Canadian chartered bank totalling $3,878 (1991 nil) for which 266,000 (1991 nil) shares of the company with a year-end market value of $6,650 (1991 nil) have been pledged as security.

5. Bank Indebtedness and Short Term Borrowings

Bank indebtedness includes $4,792 (1991 $4,315) for which a general assignment of accounts receivable and claims in process of a subsidiary of Morden & Helwig Group Inc. have been pledged as security. Short term borrowings include the current portion of long term debt of $1,532 (1991 $5,807) (note 7). Interest expense on bank indebtedness and short term borrowings amounted to $2,098 (1991 $2,012).

6. Contingent Long Term Debt

This comprises two 9.625% contingent notes payable to Federated Mutual Insurance Company for $10.2 million due March 21, 1995 and $10.2 million due March 21, 2000, which are subject to reduction based on development of unpaid claims. The shares of Federated Insurance Company of Canada and Federated Life Insurance Company of Canada, wholly owned subsidiaries of Federated Insurance Holdings of Canada Ltd., have been pledged as security for the notes. Interest expense on the contingent long term debt amounted to $1,968 (1991 $1,968).

7. Long Term Debt

The long term debt primarily consists of revolving credit facilities due in June 1997 and July 1998 and various U.S. dollar bank loans of Morden & Helwig Group Inc. at an average annual rate of 7.66% (1991 8.68%). Shares of two subsidiary insurance companies and shares of Morden & Helwig Group Inc. have been pledged as security for the loans. Interest expense on long term debt amounted to $3,507 (1991 $4,154).

Principal repayments on these loans are due as follows:

	($000)
1993	1,532
1994	1,354
1995	450
1996	435
1997 and thereafter	59,253
	63,024
Less: current portion	1,532
	61,492

8. Subordinated Convertible Debenture

On February 14, 1992 the subordinated convertible debenture was converted into 394,736 subordinate voting shares. Interest expense on the debenture at 8.5% per annum amounted to $77 (1991 $638).

9. Capital Stock

Authorized capital

The authorized share capital of the company consists of an unlimited number of preferred shares issuable in series, an unlimited number of multiple voting shares carrying ten votes per share and an unlimited number of subordinate voting shares carrying one vote per share.

Issued capital

	1992		1991	
	number	*($000)*	*number*	*($000)*
Subordinate voting shares	5,305,758	63,863	3,907,297	25,954
Multiple voting shares	1,548,000	5,000	1,548,000	5,000
	6,853,758	68,863	5,455,297	30,954
Interest in shares held through ownership interest in shareholder	(799,230)	(19,022)		
Net effectively outstanding	6,054,528	49,841	5,455,297	30,954

Under the terms of a normal course issuer bid approved by The Toronto Stock Exchange the company purchased and cancelled 109,400 (1991 21,500) subordinate voting shares for an aggregate cost of $2,644 (1991 $416), of which $1,889 (1991 $250) was charged to retained earnings. On February 14, 1992 the subordinated convertible debenture was converted into 394,736 subordinate voting shares.

On November 5, 1992 the company issued 433,773 subordinate voting shares at $28 per share as partial consideration for the purchase of Hamblin Watsa Investment Counsel Ltd.

Also on November 5, 1992, the company issued 679,352 subordinate voting shares at $28 per share to indirectly purchase 49.995% of The Sixty Two Investment Company Limited which owns 1,548,000 multiple voting and 50,620 subordinate voting shares of Fairfax. The company's indirect ownership of its own shares constitutes an effective reduction of shares outstanding by 799,230 and this effective reduction has been reflected in the fully diluted earnings per share calculation and the book value per share calculation.

10. Reinsurance

The company follows the policy of underwriting and reinsuring contracts of insurance which generally limits the liability of the company to a maximum amount on any one loss of $1 million. Reinsurance is generally placed on an excess of loss basis in several layers. This reinsurance does not relieve the company of its primary obligation to the policyholders. As at December 31, 1992 provision for claims reflects recoveries from reinsurers of $152,850 (1991 $127,140). During the year, the company ceded $67,661 (1991 $54,071) of premium income and $79,800 (1991 $59,694) of claims incurred.

11. Income Taxes

The provision for income taxes differs from the statutory marginal rate as certain sources of income are exempt from tax or are taxed at other than the marginal rate.

A reconciliation of income tax calculated at the statutory marginal tax rate with the income tax provision at the effective tax rate in the financial statements is summarized below:

	1992	1991
	($000)	*($000)*
Provision for taxes at statutory marginal income tax rate	3,093	14,382
Non-taxable investment income	(3,414)	(3,146)
Utilization of prior years' losses	(3,031)	(1,404)
Provision for (recovery of) income taxes	(3,352)	9,832

12. Statutory Requirements Insurance Subsidiaries

Payments of dividends by the company's insurance subsidiaries are governed by insurance statutes and regulations.

13. Contingencies and Commitments

Subsidiaries of the company are defendants in several damage suits and have been named as third party in other suits. The uninsured exposure to the company is not considered to be material.

The company had a joint and several agreement with a third party to guarantee two Carbovan Inc. loans totalling $11,500. The company eliminated these guarantees in 1992 and has been released from any future liability.

14. Operating Leases

Aggregate future commitments at December 31, 1992 under operating leases relating to premises, automobiles and equipment for various terms up to 10 years are as follows:

	($000)
1993	9,300
1994	7,500
1995	5,300
1996	3,500
1997	2,300
Thereafter	1,950
	$29,850

15. Earnings per Share

Earnings per share on the consolidated statements of earnings have been presented on a fully diluted basis. Basic earnings per share are $1.76 for 1992 and $4.11 for 1991. The weighted average number of shares for 1992 was 5,752,771 (1991 5,870,638) on a fully diluted basis.

16. Acquisitions

Effective October 1, 1992 the company purchased Hamblin Watsa Investment Counsel Ltd. The purchase price of $14 million was paid with $1.854 million cash and 433,773 subordinate voting shares of Fairfax Financial Holdings Limited. Hamblin Watsa Investment Counsel Ltd. had $1.1 million in total assets and $1 million in total liabilities as at October 1, 1992. The excess of the purchase price paid over the fair value of the net assets was allocated to goodwill and is being amortized over ten years. Hamblin Watsa provides discretionary investment management primarily to pension funds and to the insurance company subsidiaries of Fairfax.

On November 5, 1992 the company purchased 49.995% of the shares of The Sixty Two Investment

Company Limited (all shares other than those owned by Prem Watsa), being effectively a purchase of 799,230 shares in exchange for 679,352 subordinate voting shares of Fairfax. The only asset of Sixty Two, the controlling shareholder of the company, is 1,598,620 shares of Fairfax. As a result, the company in effect, without any payment, reduced the number of its shares outstanding by 119,878 thereby increasing its book value and earnings per share. There has been no income statement or goodwill effect as a result of this transaction.

During 1992, Morden & Helwig Group Inc., a subsidiary company, acquired various claims adjusting firms for a total consideration of $4.9 million. Virtually all of the purchase price was allocated to goodwill.

17. Related Party Transactions

During the year, the company and its subsidiaries purchased investment counselling services, in the normal course of business and on normal market terms, from Hamblin Watsa Investment Counsel Ltd., which was acquired in 1992. The cost of these services amounted to $474 in 1992 (1991 $634).

18. Segmented Information

The company is a financial services holding company which through its subsidiaries is engaged in the insurance of commercial property, oil and gas, casualty and life risks and the provision of claims adjusting and appraisal and loss management services in Canada and the United States.

(a) Industry segments

	Insurance		**Claims Adjusting, Appraisal and Loss Management**		**Corporate and Consolidation Adjustments**		**Consolidated**	
	1992 *($000)*	**1991** *($000)*	**1992** *($000)*	**1991** *($000)*	**1992** *($000)*	**1991** *($000)*	**1992** *($000)*	**1991** *($000)*
Revenue	143,915	116,038	139,782	122,982	3,133	10,982	286,830	250,002
Earnings before income taxes	7,880	28,516	1,376	2,390	(2,281)	1,559	6,975	32,465
Identifiable assets	480,066	432,694	86,441	75,488	24,041	8,382	590,548	516,564
Amortization	1,561	1,256	3,153	2,148	587	380	5,301	3,784
Interest expense	-	-	2,375	1,298	5,275	7,474	7,650	8,772

(b) Geographic segments

	Canada		United States		Total	
	1992	**1991**	**1992**	**1991**	**1992**	**1991**
	($000)	*($000)*	*($000)*	*($000)*	*($000)*	*($000)*
Revenue	177,466	166,029	109,364	83,973	286,830	250,002
Earnings before income taxes	6,654	28,168	321	4,297	6,975	32,465
Identifiable assets	424,122	361,204	166,426	155,360	590,548	516,564
Amortization	3,473	2,560	1,828	1,224	5,301	3,784
Interest expense	7,048	8,080	602	692	7,650	8,772

February 12, 1993

Auditors' Report to the Shareholders

We have audited the consolidated balance sheets of Fairfax Financial Holdings Limited as at December 31, 1992 and 1991 and the consolidated statements of earnings, retained earnings and changes in cash resources for the years then ended. These financial statements are the responsibility of the company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the company as at December 31, 1992 and 1991 and the results of its operations and the changes in its financial position for the years then ended in accordance with generally accepted accounting principles.

Coopers & Lybrand
Chartered Accountants
Toronto, Ontario

February 12, 1993

Valuation Actuary's Report

The Wyatt Company has valued the net policy (including claim) liabilities of the subsidiary general insurance companies of Fairfax Financial Holdings Limited, except for the Commonwealth Insurance Company for which we have relied upon the valuation made by J. S. Cheng & Partners Inc., in its consolidated balance sheet at December 31, 1992 and their changes as reflected in its consolidated statement of earnings for the year then ended, in accordance with accepted actuarial practice. In our opinion:

(i) the amount of the claim liabilities related to these subsidiary companies and included in the provision for claims in the consolidated balance sheet makes proper provision for future payments under these subsidiary companies' policies for the net retention on claims incurred prior to January 1, 1993; and

(ii) the valuations are appropriate, and the consolidated financial statements fairly present their results.

The Wyatt Company
Consultants and Actuaries
Toronto, Ontario

Management's Discussion and Analysis of Financial Condition and Results of Operations

Sources of Revenue

Revenue reflected in the consolidated financial statements includes premiums earned and investment income of the insurance companies, claims adjusting fees of Morden & Helwig and gains on sale of associated companies and other miscellaneous income. The following table summarizes the total revenue derived from these categories from the date of acquisition of each company for the past eight years:

Revenue by Lines of Business	**1992** *($000s)*	**1991** *($000s)*	**1990** *($000s)*	**1989** *($000s)*	**1988** *($000s)*	**1987** *($000s)*	**1986** *($000s)*	**1985** *($000s)*
Insurance	143,915	116,038	101,639	74,975	88,512	73,241	46,515	16,963
Claims adjusting	139,782	122,982	58,449	49,414	44,157	39,316	6,850	
Other income	3,133	10,982	35,342	1,365	980	414	368	52
	286,830	250,002	195,430	125,754	133,649	112,971	53,733	17,015

Insurance revenue increased by $11 million in commercial auto and $15 million in commercial property and casualty. The revenue increases in 1992 over 1991 were the result of increased prices and increased market share.

Claims adjusting revenue increased in 1992 due to Hurricane Andrew ($7.3 million) and acquisitions ($5 million).

On a geographic basis, Canadian operations accounted for approximately 62% of group revenue and 95% of group operating profits in 1992, compared with 66% of revenue and 87% of operating profits in 1991.

Net Earnings

Sources of net earnings on a pre-tax basis, with the total tax effect to the company and its consolidated subsidiaries shown as a separate item, were as follows for the past eight years:

Sources of Net Earnings by Line of Business	**1992** *($000s)*	**1991** *($000s)*	**1990** *($000s)*	**1989** *($000s)*	**1988** *($000s)*	**1987** *($000s)*	**1986** *($000s)*	**1985** *($000s)*
Insurance	7,880	30,680	6,786	(3,370)	6,468	8,539	9,594	(1,122)
Equity accounted F-M Acquisition		13,636	31,530	7,240	6,729	18		
Total	7,880	44,316	38,316	3,870	13,197	8,557	9,594	(1,122)
Claims adjusting (50% equity)	282	117	1,688	1,543	1,454	5,849	539	
Investment banking and adjustments	29	(1,058)	(6,370)	(1,439)				
Interest and corporate expenses	(4,898)	(6,516)	(9,061)	(1,499)	(2,799)	(1,668)	(353)	(277)
Realized investment gains	9,720	2,488	5,178	15,458	7,802	9,159	952	459
Provisions for investment and other losses	(6,320)	(7,000)	(7,900)					
Net earnings before taxes	6,693	32,347	21,851	17,933	19,654	21,897	10,732	(940)
Provision for income taxes	(3,352)	9,832	545	1,192	5,297	5,878	4,184	(30)
Net earnings	10,045	22,515	21,306	16,741	14,357	16,019	6,548	(910)

Net earnings in 1992 were $10 million, a decrease of $12.5 million or 56% from 1991 net earnings of $22.5 million.

The major changes which affected net earnings before taxes were:

Insurance underwriting results declined by $22.2 million from 1991

Insurance interest and dividend income decreased by $2.6 million from 1991

1991 reflects a gain on the sale of F-M Acquisition of $13.6 million

The equity share of claims adjusting net earnings increased by $0.2 million from 1991

Investment banking expenses and adjustments decreased by $1.1 million

The tax provision changed to a refund of $3.4 million versus the 1991 provision of $9.8 million (effective rate 30.4%) because of previous years' loss carry forwards and deductions and a change in the investment income mix.

Insurance Underwriting

Fairfax's insurance companies employ disciplined underwriting practices with the objective of rejecting underpriced risks. The combined loss and expense ratio is the traditional measure of underwriting results of property and casualty companies. In any year when the ratio exceeds 100%, it generally indicates that unprofitable business has been underwritten.

A summary follows of the net premiums written and earned, and the loss, expense and combined ratios, for each of the past eight years.

	NET PREMIUMS		RATIOS		
	Written	**Earned**	**Losses**	**Expenses**	**Combined**
	($000s)	*($000s)*	*(%)*	*(%)*	*(%)*
1985	23,415	14,049	96	30	126
1986	55,992	40,885	72	23	95
1987	71,378	62,012	73	25	98
1988	68,224	66,265	73	19	92
1989	35,477	40,444	100	40	140
1990	74,487	78,427	82	31	113
1991	93,450	90,507	60	34	94
1992	128,664	118,854	79	35	114

In 1992 the loss ratio increased as a result of losses related to Hurricane Andrew and two lines of business we terminated in that year.

Net premiums written and earned by line for the past five years are shown in the following table:

		1992	**1991**	**1990**	**1989**	**1988**
Operational area		*($000s)*	*($000s)*	*($000s)*	*($000s)*	*($000s)*
Commercial auto, general liability	Written	28,551	13,190	15,654	28,795	41,677
	Earned	24,481	13,042	19,938	31,980	42,006
Farm and reinsurance run off	Written	9,871	9,969	10,393	6,682	26,547
	Earned	9,279	7,552	10,287	8,464	24,259
Direct commercial lines	Written	38,923	37,249	40,012		
	Earned	38,776	38,838	40,858		
Commercial property and	Written	51,319	33,042	8,428		
casualty	Earned	46,318	31,075	7,344		
Totals	Written	128,664	93,450	74,487	35,477	68,224
	Earned	118,854	90,507	78,427	40,444	66,265

Commercial auto and direct commercial premium volume has increased due to price increases and market share recovery.

Farm and reinsurance run off premium has remained constant since the book of business of the reinsurance company was sold in 1989. In 1992 the farm insurance book was sold.

Commercial property and casualty premium shows an increase in 1991 as a result of the timing of the acquisition in 1990. 1991 reflects a full year of operation under Fairfax. 1992 increases are mainly the result of increased submissions and higher retentions.

The total underwriting profit (loss) by line for the insurance companies for the past five years is shown in the following table:

	1992	**1991**	**1990**	**1989**	**1988**
	($000s)	*($000s)*	*($000s)*	*($000s)*	*($000s)*
Commercial auto, general liability	(3,982)	6,121	(8,708)	(12,964)	1,172
Farm and reinsurance run off	(1,018)	(1,181)	(327)	1,049	(822)
Direct commercial lines	(1,924)	184	(2,472)		
Commercial property and casualty	(9,959)	196	(997)		
	(16,883)	5,320	(12,504)	(11,915)	350

The losses in commercial auto and general liability in 1989 and 1990 were the result of surety losses and that book of business was discontinued in 1990. The underwriting profit in 1991 in commercial auto and general liability was primarily a result of recoveries related to surety business. The underwriting loss in 1992 related mainly to terminated lines of business.

Direct commercial lines declined slightly from 1991. Commercial and casualty lines were unfavourably affected by Hurricane Andrew for approximately $11 million.

Provision for claims

Claim provisions are established by the case method as claims are reported. The provisions are subsequently adjusted as additional information on the estimated amount of a claim becomes known during the course of its settlement. A provision is also made for management's calculation of factors affecting the future development of claims including claims incurred but not reported (IBNR) based on the volume of business currently in force and the historical experience on claims.

As time passes, more information about the claims becomes known and provision estimates are appropriately adjusted upward or downward. Because of the estimation elements encompassed in this process, and the time it takes to settle many of the more substantial claims, several years are required before a meaningful comparison of actual losses to the original provisions can be developed.

The development of the provision for claims is shown by the difference between estimates of reserves as of the initial year-end and the re-estimated liability at each subsequent year-end. This is based on actual payments in full or partial settlement of claims, plus re-estimates of the reserves required for claims still open or claims still unreported. Favourable development means that the original reserve estimates were higher than subsequently indicated. Unfavourable development means that the original reserve estimates were lower than subsequently indicated.

The table below shows the original provision for claims reserves including loss adjustment expense (LAE) at each calendar year-end with the subsequent cumulative payments made from these years and the subsequent re-estimated amount of these reserves. The following insurance subsidiaries' reserves are included in the year in which they were originally acquired.

Subsidiary	Year Acquired
Markel Insurance Company of Canada	1985
Sphere Reinsurance/Chequers Insurance Company	1986
Otter Dorchester Insurance Company	1987
Federated Insurance Company of Canada	1990
Commonwealth Insurance Company	1990

Provisions ***(s/b provisiON - singular?)*** *for Claims Reserve Development*
*Markel, Federated and Commonwealth**
($000s)

As of December 31	1985 and prior	1986	1987	1988	1989	1990	1991	1992
Provisions for claims including LAE	17,517	39,522	59,400	71,964	79,357	192,372	168,394	179,588
Cumulative payments as of:								
One year later	8,069	13,940	18,752	21,015	25,194	44,055	48,050	
Two years later	11,822	22,613	27,154	33,196	35,440	76,947		
Three years later	15,514	27,295	32,919	42,043	44,169			
Four years later	16,313	30,156	37,784	47,901				
Five years later	16,989	33,256	41,128					
Six years later	16,989	34,928						
Seven years later	16,989							
Reserves re-estimated as of:								
One year later	18,596	42,907	56,920	71,673	80,602	175,138	168,001	
Two years later	18,352	43,397	54,920	69,930	73,904	173,992		
Three years later	19,210	43,148	53,004	67,676	71,810			
Four years later	19,079	41,448	52,295	64,478				
Five years later	18,613	41,730	50,235					
Six years later	16,989	40,280						
Seven years later	16,989							
Favourable (unfavourable) development	528	(758)	9,165	7,486	7,547	18,380	393	

* *Wentworth Insurance Company and Federated Life Insurance Company of Canada are not included.*

While management is pleased with the favourable development over the past five years, future development can be significantly different from the past due to many unknown factors.

The following table shows the provision for claims liability for unpaid losses and LAE as originally estimated for the years 1990 through 1992, the amounts paid with respect to the reserves for each subsequent year, the re-estimated liability at the end of each year, and the resulting development from prior years. The favourable or unfavourable development from prior years is credited or charged to each year's earnings.

Reconciliation of Provisions for Claims
*Markel, Federated and Commonwealth**
($000s)

	1992	1991	1990
Provision for claims and LAE at January 1	168,394	192,372	79,357
Plus provision for claims of purchased subsidiaries at their purchase dates			85,428
	168,394	192,372	164,785
Incurred losses on claims and LAE			
Provision for current accident year claims	94,177	63,163	80,199
Increase (decrease) in provision for prior accident years' claims	(393)	(17,234)	1,245
Total incurred losses on claims and LAE	93,784	45,929	81,444
Payments for losses and LAE			
Payments on current accident year claims	(34,540)	(25,852)	(28,663)
Payments on prior accident years' claims	(48,050)	(44,055)	(25,194)
Total payments for losses and LAE	(82,590)	(69,907)	(53,857)
Provision for claims and LAE at December 31	179,588	168,394	192,372

** Wentworth Insurance Company and Federated Life Insurance Company of Canada are not included.*

As shown in the table, there has been favourable development from prior years of about $0.4 million in 1992 and $17.2 million in 1991, and unfavourable development of $1.2 million in 1990 (mainly because of surety losses in 1989).

The company strives to establish adequate provisions at the original valuation date. While the favourable development from prior years in the past two years is comforting, the company continues to be subject to upward or downward development in the future.

Insurance Environment

The property and casualty insurance market in general experienced another year of poor underwriting results with combined ratios in Canada expected to be approximately 110% for 1992. Many insurance companies continue to write insurance at inadequate prices. Following the various very large underwriting losses incurred in 1992 in the U.S. and Europe, price adjustments appear inevitable.

Interest and Dividend Income

The majority of interest and dividend income is earned by the insurance companies. The Commonwealth and Federated acquisitions added $129.8 million and $100.8 million respectively to the investment portfolio at the end of 1990, and interest and dividend income for Commonwealth was included for only two months in 1990.

	Average Investments at Book Value ($000s)	Interest and Dividend Income ($000s)	Income Yield (%)
1985	29,060	2,455	8.45
1986	64,181	4,678	7.29
1987	109,825	8,042	7.32
1988	130,782	8,922	6.82
1989	135,703	11,628	8.57
1990	237,868	20,704	8.70
1991	338,461	26,051	7.70
1992	366,481	23,988	6.55

The income yield declined in 1992 to 6.55% as a result of the decline in interest rates and also a switch from bonds into high quality preferreds. Investments for the past eight years are shown in the following table, at the average of their carrying values at the beginning and end of each year:

	Cash and Short Term Investments ($000s)	Bonds ($000s)	Preferreds ($000s)	Common ($000s)	Total ($000s)
1985	10,526	15,388	732	2,414	29,060
1986	16,605	24,523	7,979	15,074	64,181
1987	28,025	26,242	16,516	39,042	109,825
1988	29,843	23,575	25,191	52,173	130,782
1989	20,623	28,528	32,212	54,340	135,703
1990	33,596	99,220	45,652	59,400	237,868
1991	60,099	140,177	75,685	62,500	338,461
1992	77,929	108,818	99,821	79,913	366,481

Return on Investment Portfolio

The following table shows the performance of the investment portfolio for the past eight years. The total return includes all interest and dividend income, gains (losses) on the disposal of securities and the change in the unrealized gains (losses) during the year.

	Average Investments at Book ($000s)	Dividends and Interest Earned ($000s)	Realized Gains (Losses) After Provisions ($000s)	Change in Unrealized Gains (Losses) ($000s)	Total Return on Average Investment ($000s)	Percentage Return
1985	29,060	2,455	459	878	3,792	13
1986	64,181	4,678	952	(352)	5,278	8
1987	109,825	8,042	9,159	(7,976)	9,225	8
1988	130,782	8,922	7,802	12,131	28,855	22
1989	135,703	11,628	15,458	(6,272)	20,814	15
1990	237,868	20,704	2,278	(32,943)	(9,961)	(4)
1991	338,461	26,051	(4,512)	27,866	49,405	15
1992	366,481	23,988	3,400	(11,197)	16,191	4

Investment gains (losses) have been an important component of Fairfax's net earnings since 1985. The amount has fluctuated significantly from period to period, but the amount of investment gains (losses) for any period have no predictive value and variations in amount from period to period have no practical analytical value. The gains (losses) on investments recorded in the statement of earnings for 1992 are net of provisions for losses on investments of $6.4 million (1991 $7 million). At December 31, 1992 the aggregate provision for losses on investments was $16.3 million (1991 $9.9 million). At December 31, 1992 the Fairfax investment portfolio had an unrealized loss of $17.4 million compared to an unrealized loss at December 31, 1991 of $6.1 million.

The company expects continuing fluctuations in the stock market and continues to maintain its long term value-oriented investment philosophy.

Capital Resources

At December 31, 1992 total capital funds, comprising shareholders' equity and non-controlling (minority) interest, were $161.2 million, compared to $141.3 million (including the subordinated convertible debenture) at December 31, 1991.

The following table shows the level of capital as at December 31 for the last four years:

			($000s)	
	1992	**1991**	**1990**	**1989**
Non-controlling interest	17.4	17.0	16.7	10.7
Subordinated convertible debenture		7.5	7.5	7.5
Shareholders' equity	143.8	116.8	94.7	90.8
	161.2	141.3	118.9	109.0

Fairfax's consolidated balance sheet as at December 31, 1992 reflects a significant improvement in capital strength from 1991. Fairfax shareholders' equity has increased from $116.8 million at December 31, 1991 to $143.8 million at December 31, 1992. In 1992 the company purchased and cancelled 109,400 subordinate voting shares at an average price of $24.12. Also, on February 14, 1992 the $7.5 million subordinated convertible debenture was converted into 394,736 subordinate voting shares, increasing shareholders' equity to over $124 million. Effective October 1, 1992, the company purchased Hamblin Watsa Investment Counsel Ltd. The purchase price of $14 million was paid with $1.854 million cash and 433,773 subordinate voting shares valued at $28 per share.

On November 5, 1992, the company issued 679,352 subordinate voting shares at $28 per share to indirectly purchase 49.995% of The Sixty Two Investment Company Limited which owns 1,598,620 shares of Fairfax. Fairfax's indirect ownership of its own shares through The Sixty Two Investment Company Limited results in an effective reduction of shares outstanding by 799,230, and this reduction has been reflected in the fully diluted earnings per share calculation and the book value per share calculation.

In November 1992 Fairfax received approval from The Toronto Stock Exchange to purchase up to 454,500 subordinate voting shares of the company under a normal course issuer bid. None had been purchased at December 31, 1992.

Liquidity

The purpose of liquidity management is to ensure that there is sufficient cash to meet all financial commitments and obligations as they fall due.

Fairfax has the financial flexibility to obtain from internal or external sources the funds needed to fulfil its cash requirements during the current financial year. Cash requirements for Fairfax on an entity basis in 1993 include debt servicing and administration expense, totalling about $6 million. Total dividends available from regulated insurance companies in 1993 are approximately $12 million. The insurance subsidiaries of Fairfax are regulated in their various jurisdictions of operation. As at December 31, 1992 all our insurance companies met the standards set by the applicable regulatory authorities.

Consolidated interest expense decreased in 1992 to $7.7 million from $8.8 million in 1991 due to lower interest rates.

During 1992, long term debt at Fairfax increased $17 million at the entity level and $6 million at the Morden & Helwig level. The company received smaller dividends in 1992 from its insurance companies, and funded $6 million of commitments it had agreed to in past years. In addition, Morden & Helwig and Fairfax completed several acquisitions which led to the debt increase.

As a result, the debt to equity ratio with Morden & Helwig equity accounted increased to 0.47:1 at December 31, 1992 compared to 0.44:1 at December 31, 1991. The company expects to reduce debt by approximately $17 million in 1993, barring any acquisition activity.

The company has not paid and does not intend to pay dividends as long as it can reinvest the funds and earn a 20% return on equity over time.

At December 31, 1992 Fairfax had $75 million of revolving five year term lines of credit of which $47 million was utilized.

Fairfax Insurance Companies

Combined Statements of Earnings
for the years ended December 31, 1992 and 1991
(unaudited)

	1992	1991
	($000)	*($000)*
Revenue		
Premiums earned	118,854	90,507
Interest and dividends	22,786	25,361
Realized gains (losses) on investments	1,977	(2,165)
Other income	298	2,335
	143,915	116,038
Expenses		
Losses on claims	94,457	54,267
Operating expenses	37,671	33,606
Commissions, net	3,907	(351)
	136,035	87,522
Earnings before income taxes	7,880	28,516
Provision for (recovery of) income taxes	(4,171)	7,676
Net earnings	12,051	20,840

Fairfax Insurance Companies

Fairfax's insurance business is conducted by five subsidiaries. The companies underwrite a wide range of commercial property and oil and gas insurance in Canada, the United States and internationally as well as commercial casualty, commercial truck and smaller amounts of property, casualty, life, health and disability insurance in Canada.

Fairfax Insurance Companies

Combined Balance Sheets
as at December 31, 1992 and 1991
(unaudited)

	1992	1991
	($000)	*($000)*
Assets		
Cash and short term investments	83,109	72,141
Accounts receivable	73,390	71,802
Income taxes refundable	5,448	
	161,947	143,943
Portfolio investments		
Bonds at book value	103,318	114,506
Preferred stocks at book value	109,483	94,100
Common stocks at book value	92,246	64,409
	305,047	273,015
Deferred premium acquisition costs	6,307	6,128
Capital assets	6,684	5,545
Other assets	82	2,650
	480,067	431,281
Liabilities		
Accounts payable and accrued liabilities	31,650	22,681
Premium deposits	5,844	3,993
Income taxes payable		2,441
	37,494	29,115
Provision for claims	208,762	194,927
Unearned premiums	66,135	55,044
Deferred income taxes	6,936	5,706
	281,833	255,677
Shareholders' Equity	160,740	146,489
	480,067	431,281

Fairfax with Equity Accounting of Morden & Helwig
Consolidated Balance Sheets

as at December 31, 1992 and 1991
(unaudited)

	1992	**1991**
	($000)	*($000)*
Assets		
Cash and short term investments	83,011	72,038
Accounts receivable	73,098	74,235
Income taxes refundable	4,964	
Prepaid expenses	2,416	2,132
	163,489	148,405
Portfolio investments		
Bonds		
(market value $105,637; 1991 $114,086)	103,224	114,412
Preferred stocks		
(market value $108,412; 1991 $91,262)	106,779	92,100
Common stocks		
(market value $76,701; 1991 $56,934)	97,902	61,924
Total (market value $290,750; 1991 $262,282)	307,905	268,436
Investment in Morden & Helwig	25,186	24,874
Other investments	4,459	4,651
Deferred premium acquisition costs	6,307	6,128
Capital assets	6,801	5,635
Goodwill	13,640	
Other assets	4,279	9,888
	532,066	468,017
Liabilities		
Bank indebtedness		165
Accounts payable and accrued liabilities	32,336	23,174
Premium deposits	5,844	3,993
Income taxes payable		2,441
	38,180	29,773
Provision for claims	208,816	202,120
Unearned premiums	66,135	55,044
Contingent long term debt	20,445	20,445
Long term debt	47,736	30,654
Deferred income taxes	6,936	5,706
	350,068	313,969
Subordinated convertible debenture		7,500
Shareholders' Equity		
Capital stock	49,841	30,954
Retained earnings	93,977	85,821
	143,818	116,775
	532,066	468,017

Morden & Helwig Group Inc.
Consolidated Balance Sheets
as at December 31, 1992 and 1991

	1992 ($000)	1991 ($000)
Assets		
Cash	484	324
Accounts receivable	25,128	20,640
Claims in process	12,391	12,523
Prepaid expenses	1,227	1,249
	39,230	34,736
Notes receivable	1,143	1,108
Capital assets	10,622	8,952
Other assets	35,446	30,692
	86,441	75,488
Liabilities		
Bank indebtedness	4,792	4,315
Accounts payable and accrued liabilities	14,017	10,546
Income taxes payable	278	35
Long term debt current portion	1,532	5,807
Deferred income taxes	3,024	3,160
Net liabilities of discontinued operations	64	268
	23,707	24,131
Long term debt	13,336	3,869
Future retirement payments	6,384	5,758
	19,720	9,627
Subordinated convertible debenture	8,320	7,900
Shareholders' Equity		
Capital stock	22,625	21,831
Retained earnings	12,069	11,999
	34,694	33,830
	86,441	75,488

Morden & Helwig Group Inc.
Consolidated Statements of Earnings
for the years ended December 31, 1992 and 1991

	1992 ($000)	1991 ($000)
Revenue	139,294	122,460
Cost and expenses		
Cost of service	108,084	94,337
Selling, general and administration	27,480	23,059
Interest	2,375	1,298
Gain on disposal of assets	(21)	(595)
	137,918	118,099
Earnings before income taxes	1,376	4,361
Income taxes	814	2,156
Earnings from continuing operations	562	2,205
Discontinued operations		(1,971)
Net earnings	562	234

Consolidated Statements of Retained Earnings
for the years ended December 31, 1992 and 1991

	1992 ($000)	1991 ($000)
Retained earnings - beginning of year	11,999	12,257
Net earnings for the year	562	234
Dividends	(492)	(492)
Retained earnings - end of year	12,069	11,999

These condensed financial statements have been prepared from the Morden & Helwig Group Inc. audited consolidated financial statements for the years ended December 31, 1992 and 1991, copies of which are available on request.

Consolidated Financial Summary *(in thousands except per share data)*

	1992	1991	1990	1989	1988	1987	1986	1985	1984	1983
	For the years ended December 31									
Operating Results										
Premiums earned	118,854	90,507	78,427	40,444	66,265	62,012	40,885	14,049	16,616	19,621
Claims fees	139,782	122,982	58,281	49,092	43,349	33,529	6,850			
Interest and dividends	23,988	26,051	20,704	11,628	8,922	8,042	4,678	2,455	2,337	2,009
Realized gains (losses) on investments	3,400	(4,512)	2,278	15,458	7,802	9,159	952	459	25	215
Other income	806	14,974	35,740	9,132	7,311	229	368	52		
Total revenue	286,830	250,002	195,430	125,754	133,649	112,971	53,733	17,015	18,978	21,845
Earnings before income taxes	6,975	32,465	23,238	19,204	21,324	18,203	9,085	(880)	(4,854)	308
Extraordinary items						1,700	1,711			
Net earnings	10,045	22,515	21,306	16,741	14,357	16,019	6,548	(910)	(4,775)	280
Per Common Share										
Net earnings fully diluted	1.76	3.94	2.92	2.25	1.94	2.23	1.35	(1.89)	(7.75)	0.45
Shareholders' equity	23.76	21.41	17.29	12.41	10.13	8.32	5.89	2.08	3.71	11.46
Number of shares outstanding year-end	6,055	5,455	5,477	7,316	7,322	7,337	7,007	5,000	616	616
Financial Condition										
Total Assets	590,548	516,564	535,987	248,065	246,786	185,413	129,845	41,477	31,401	32,325
Cash and investments	391,781	341,180	335,740	133,858	137,548	124,016	95,633	32,728	25,391	24,218
Total debt *	68,181	51,264	65,918	21,988	28,235	2,773	2,800		1,000	300
Shareholders' equity	143,818	116,775	94,676	90,830	74,176	61,048	41,275	10,379	2,287	7,062
Return on Average Shareholders' Equity	**7.7%**	**21.3%**	**23.0%**	**20.3%**	**21.2%**	**31.3%**	**25.4%**			**4.1%**

* Total debt with Morden & Helwig equity accounted

Readers of this Management's Discussion and Analysis should review the entire annual report for additional commentary and information.

Directors of the Company

H. Anthony Arrell
Chairman and Chief Executive Officer
Burgundy Asset Management Ltd.

Winslow W. Bennett
President, Winwood Holdings Ltd.

Robbert Hartog
President, Robhar Investments Ltd.

Steven A. Markel
Vice Chairman and Treasurer,
Markel Corporation

Kenneth R. Polley
President and Chief Executive Officer,
Morden & Helwig Group Inc.

John C. Puddington
President, Trilwood Investments Limited

V. Prem Watsa
Chairman and
Chief Executive Officer

Audit Committee Member

Operating Management

John B. O. Watson
President
Commonwealth Insurance Company

John M. Paisley
President
Federated Insurance Company of Canada
and
Federated Life Insurance Company of Canada

Anthony F. Hamblin
President
Hamblin Watsa Investment Counsel Ltd.

William S. Grant
President
Markel Insurance Company of Canada

Kenneth R. Polley
President
Morden & Helwig Group Inc.

Officers of the Company

Brenda Adams
Corporate Secretary

Sam Chan
Vice President

J. Paul T. Fink
Vice President

Eric P. Salsberg
Vice President, Corporate Affairs

Ronald Schokking
Vice President, Finance

John C. Varnell
Vice President and
Chief Financial Officer

V. Prem Watsa
Chairman and Chief Executive Officer

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Transfer Agent and Registrar
The R-M Trust Company

Share Listing
The Toronto Stock Exchange
Exchange Symbol FFH

General Counsel
Tory Tory DesLauriers & Binnington

Auditors
Coopers & Lybrand

Annual Meeting
The annual meeting of shareholders of
Fairfax Financial Holdings Limited
will be held on Wednesday, May 12, 1993
at 4.30 p.m. at The Toronto Stock
Exchange