FAIRFAX
FINANCIAL HOLDINGS LIMITED

1995 Annual Report

Contents

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Five Year Financial Highlights

(in $ millions except share and per share data)

	1995	1994	1993	1992	1991
Revenue	1,145.5	634.9	344.0	286.8	250.0
Net earnings	87.5	38.1	33.3	10.0	22.5
Total assets	2,332.9	2,173.4	1,200.3	590.5	516.6
Shareholders' equity	472.6	391.9	279.5	143.8	116.8
Shares outstanding year-end *(mil.)*	8.9	9.0	8.0	6.1	5.5
Return on average equity	20.1%	12.1%	20.3%	7.7%	21.3%
Per share					
Net earnings fully diluted	9.79	4.66	5.42	1.76	3.94
Shareholders' equity	53.28	43.77	35.13	23.76	21.41
Market prices per share					
High	100.00	76.00	61.25	30.00	22.50
Low	66.25	52.00	24.00	21.75	10.75
Close	98.00	67.00	61.25	25.00	21.25

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, offers commercial property and oil and gas insurance in Canada, the United States and internationally, and commercial casualty insurance in Canada. In 1995 Commonwealth's net premiums written totalled $87.9 million. Commonwealth has been in business since 1947 and at year-end there were 138 employees.

Federated Insurance is based in Winnipeg. Its two companies market a broad range of insurance products primarily for commercial customers. In 1995 Federated's net premiums written totalled $57.6 million, consisting of $47.2 million of property and casualty business and $10.4 million of life and group health and disability products. Federated has been in business since 1920 and at the end of 1995 had 246 employees.

Lombard Insurance (formerly called Continental Insurance), based in Toronto, writes a complete range of commercial and personal insurance products. The company has been in business since 1904. In 1995 Lombard's net premiums written were $351.6 million. At year-end there were 716 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. In 1995 net premiums written were $79.7 million and the company had 90 employees at year-end.

Ranger Insurance, based in Houston, Texas, specializes in writing property and casualty insurance to niche markets in the United States such as propane distributors, petroleum and gas marketers and agri-products. The company has been in business since 1923. In 1995 Ranger's net premiums written were US$131.4 million. At year-end there were 295 employees.

CRC (Bermuda) Reinsurance, based in Bermuda, continues to reinsure Lombard Insurance on the same basis as its previous owner did. The company received its insurance certificate early in 1995 and had net premiums written in 1995 of $92.3 million.

Wentworth Insurance was incorporated in 1990 as an insurance company domiciled in Barbados. In 1995 Wentworth's net premiums written were $15.4 million. At year-end there were 6 employees.

Lindsey Morden Group (formerly Morden & Helwig Group) is engaged in providing claims adjusting, appraisal and loss management services to a wide variety of insurance companies and self-insured organizations across Canada and the United States. In 1995 revenue totalled $154.9 million. The company was established in 1923, and at year-end the group had 1,625 employees located in 287 offices.

Hamblin Watsa Investment Counsel 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 $2.3 billion.

Note: All companies are wholly owned except Lindsey Morden Group, a public company of which Fairfax owns 57% of the equity and 92% of the votes.

To Our Shareholders

We just made it. With the help of strong financial markets, we barely cleared our 20% return on equity hurdle. We earned 20.1% on average shareholders' equity in 1995 (versus 12.4% for the TSE 300). Reflecting our larger equity base, we made record earnings on an absolute and on a per share basis. Net income after tax in 1995 increased by 130% to $87.5 million. In spite of the 9% increase in the average number of shares outstanding, earnings per share increased by 110% to $9.79. Book value per share increased by 22% to $53.28 while the share price closed at $98.00, up 46% in 1995. While our shares did trade at $100, we were hoping they would close the year at $100 so that your future analysis of our compound growth would be much easier. Don't throw out that calculator yet!

1995 marks the end of Fairfax's first decade. Since we began in September 1985, our results have been much better than we expected and are quite humbling when we consider all the mistakes that we have made over this time period. And for sure, our results will not be repeated. In its first decade, Fairfax has earned an average annual return on shareholders' equity of 20.3% (versus 7.5% for the TSE 300), pretty well right on our 20% objective. However, book value per share has increased by more than 25 times while the stock price has increased by 30 times. We began with one insurance company, Markel Insurance, with annual premiums in 1985 of $17 million. Today we have seven insurance companies, an investment counselling operation and a claims adjusting company, with revenue in excess of $1 billion (insurance premiums of $829 million). In 1985 the company had never earned $1 million in its past. In 1995 we earned $87.5 million. Investable assets increased from $33 million in 1985 to $1.7 billion in 1995. This record was achieved while always maintaining a strong financial position, and we ended the decade in the strongest financial position we have ever had.

While we are very gratified by these results, we are even more grateful for the fact that they were achieved by treating our customers, employees and shareholders and others that we deal with in a fair and friendly way. This approach to business may penalize our results in the short term, but it is the only one we feel comfortable with and the way you can expect us to behave in the future.

How does Fairfax's record rank among Canadian businesses? As disclosed annually, the Report on Business Magazine (July 1995 issue) ranks Fairfax's five year average ROE at 59 (or 51 on the basis of our calculations) out of the top 1000 companies listed on the Canadian stock exchanges, i.e. in the top 5-6% of all companies in Canada. Our own analysis suggests that for the nine years ending December 31, 1994 (those are the latest figures that are available), Fairfax's average ROE of 20.3% was the ninth best of all the TSE 300 companies. In terms of share price growth and book value growth for the same period, Fairfax was fourth best among the TSE 300 companies (rest assured we won't tell you who was ranked higher!!). So you can see that 20% is an extremely challenging objective for us and one that we will continue to strive for in the next five years. Our past record of 40% annual compound growth in stock price and book value, as we have repeated *ad nauseam*, is not repeatable in the future.

Besides earning 20.1% on shareholders' equity in 1995, our most significant accomplishment was our strong year-end financial position. We did our second U.S. debt financing, led again by J.P. Morgan and First Boston. We issued US$100 million of unsecured debentures with an 8¼% coupon and a 20 year term to maturity. While we were happy with the absolute rate, the spread of 170 basis points over comparable treasuries was a little higher than we expected. The rating agencies (Standard & Poor's, Duff & Phelps and Dominion Bond Rating Service) all upgraded us to a BBB+ before the issue. Unfortunately, late in the year Moody's rained on our parade with a Baa3 rating on our debentures. We welcome our debenture investors and want to reassure them that we run our company at standards that merit an A, and we hope to convince the rating agencies of that soon. Proceeds from the debenture issue repaid our long term bank debt and also left us with about $70 million cash in the parent company. By year-end, we had raised our unused, unsecured, committed, long term bank lines to $215 million from $105 million. Our debenture issue and increased bank lines resulted in Fairfax being in the strongest financial position it has ever been in during its ten year history. Our small head office at Fairfax, led by Rick Salsberg and John Varnell and ably supported by Brenda Adams, Sam Chan and Ronald Schokking, took all of this in stride.

We commented in our 1994 Annual Report that although our share issue in 1994 at $76 was $12 above the previous day's trade, it was a fair price for our shares over the long term. We said we were "concerned with making our investors look good in the long term". While a year is certainly not the long term and if our shares had not gone up in 1995 we would not be making this comment our shares have gone up by 29% from the issue price, significantly higher than the 8% for the TSE 300. Our focus continues to be the long term.

With our shares now trading at three digits, we are often asked about stock splits for greater liquidity, higher stock prices, etc., etc. We have always replied in the negative. Our view is that stock splits do not make shares more or less valuable; they just increase the number of slices that you take from a cake but do not increase the size of the cake. Our focus is to increase the long term intrinsic value of our company (the cake) and not change the number of slices. Together with our dividend policy (no dividends), investor relations department (none) and lack of emphasis on short term (quarterly) earnings, we have instituted policies that cater to the long term investor, i.e. investors who buy and hold our shares for the long term. Have we been successful in attracting this type of investor? During 1995 1.5 million shares of Fairfax were traded on the TSE, or approximately 20% of the public float. When compared to the companies in the TSE 300, Fairfax's turnover (shares traded as a percentage of the float) in 1995 was ranked eighth from the bottom exactly where we want to be!! The highest turnover on the TSE was 1250%, the lowest 13% and the average 60%. Sell your shares if we ever make the TSE options list.

While we are discussing the long term, we should remind you (as we did in our 1986 Annual Report) that you have one significant short term disadvantage by my controlling all the multiple voting shares. I will not sell my shares even at a 100% premium to current prices (i.e. $200 per share) and thus my multiple voting shares prevent you from getting an attractive one time bonanza. However, for this short term pain, we hope to provide you with good long term gains. In case you forgot the power of compounding, a 20% ROE over 13 years (with no dividends) results in a tenfold increase in book value (and may I dare say, stock prices?!). While we have more than achieved this in the past, the future is definitely not guaranteed.

As we are discussing my shares, you should know that I have arranged my affairs so that my death (not expected soon!) will not trigger the sale of any of my multiple voting shares. No short term bonanza even at my passing away!

With Fairfax at $100 per share, many of you are probably wondering if this is as good as it gets. Is the stock overvalued and can it drop significantly? This is a good question and you will have to come to your own conclusion based on the facts that we have disclosed in this Annual Report. However, you should recognize the following:

1) Stock prices will always fluctuate including Fairfax's. They can easily go down 50% from current levels but as long as you don't have to sell, you will not lose money.
2) At $100, the shares are selling at approximately twice book value, close to the top of their historical range. In relation to earnings, the shares are trading at approximately ten times significantly less than the 13.8 times and 17.8 times for the TSE 300 and S&P 500 respectively.
3) In the past decade, stock price growth has followed growth in book value irregularly and over time.
4) Our book values are very conservatively stated but they are a first proxy for intrinsic value or what the company is worth. While you should make your own estimate of intrinsic value, it is fair to say that in 1995 the intrinsic value of Fairfax increased by at least the same percentage as the increase in book value.

So I really don't know what stock prices will do in the short term never have but I suggest taking the long view.

While we are talking about the long view, you will be happy to hear that at Fairfax, we eat our own cooking. All of the key officers of Fairfax (including yours truly), the partners of Hamblin Watsa and the presidents of our subsidiaries have a very significant portion of their net worth in Fairfax shares. At least three out of our six directors also have a meaningful investment in Fairfax. In total, over 21% of all Fairfax shares are owned by the directors, officers and employees of Fairfax. At $100 per share, this works out to approximately $189 million. So if you ever get indigestion when you look at our stock price in the financial pages, it may help to know we are suffering too!
The table below shows the sources of our net earnings:

		($ millions)
	1995	**1994**
Insurance underwriting	(40.9)	(16.9)
Interest and dividends	86.3	53.8
Total	45.4	36.9
Claims adjusting (Fairfax portion)	2.1	0.5
Interest expense	(19.1)	(10.4)
Goodwill amortization	(1.4)	(1.4)
Corporate overhead and other	(9.0)	(2.1)
Realized gains	71.9	20.0
Pre-tax income	89.9	43.5
Less: taxes	2.4	5.4
Net earnings	87.5	38.1

The table shows you the results from our insurance (underwriting and investments) and non-insurance operations. Claims adjusting shows you our share of Lindsey Morden's after-tax income. The corporate overhead expense is net of Hamblin Watsa's pre-tax income. Shown separately are realized gains so that you can better understand our earnings from our operating companies. Also please note the unaudited financial statements of our combined insurance operations and of Fairfax with Lindsey Morden equity accounted, as well as Lindsey Morden's financial statements, shown on pages **XX**.

The significant increase in the underwriting loss in 1995 was largely due to Ranger, and secondly, Lombard. Interest and dividend income as well as interest expense increased because of the Lombard acquisition in 1994. Lindsey Morden made a significantly higher contribution to our earnings in 1995. Corporate overhead and other increased mainly because of one time expenses associated with the debt issue, the start-up of our reinsurance division in New York, reduced income from Hamblin Watsa and other expenses. As the table shows clearly, realized gains were the main reason for the large net earnings increase in 1995. Taxes continued at lower levels because of the utilization of available losses and loss carry forwards, a greater amount of tax-free Canadian dividend income, and higher income from lower taxed non-North American operations.

Insurance operations

1995 worked out to be an excellent year for our Canadian insurance companies but not so for Ranger. Overall, we had a combined ratio of 104.9% for 1995 versus 104.2% in 1994. Excluding Ranger, our insurance companies had a combined ratio of 101% while Ranger had a combined ratio of 118.1% (after indemnifications). Since 1985 we have achieved our target combined ratio of 100% or less in only five of the last ten years a .500 record which in baseball would be terrific but is nothing to write home about in the insurance industry.

Commonwealth, led by John Watson, continued to produce excellent results. Commonwealth had a superb 1995 with a combined ratio of 89.5% versus a Northridge-plagued 97.8% in 1994. Underwriting profit in 1995 was about $9.1 million. Since we purchased it in 1990, this company has had a combined ratio of less than 100% in every year except 1992 (Hurricane Andrew), i.e. four out of five great years. Recently, Standard & Poor's upgraded Commonwealth to an A from A and Duff & Phelps to an A+ from an A, while A.M. Best continues to rate Commonwealth at an A (excellent).

Gross premiums at Commonwealth increased to a record $291 million from $263 million in 1994, while net premiums earned remained flat at $87 million. Net income after taxes was a record $20.2 million versus $17.5 million in 1994. While premiums increased in every division in 1995, there are growing signs that pricing in the oil and gas and petroleum sector has peaked. Canadian property, casualty and U.S. property divisions have all firmed but are still very competitive.

Commonwealth continues to very carefully monitor its exposure to catastrophes through the Insurance Risk Assessment System program. As mentioned in earlier Annual Reports, we remain exposed to the unlikely possibility of a major catastrophe impacting the income statement of Commonwealth but not, we feel, its balance sheet.

1995 was the first full year for Lombard (which used to be known as Continental) under Fairfax's ownership. Led by Byron Messier and his management team, Lombard had an excellent first year with a normalized combined ratio of 103% (after indemnification). During the year, Byron split the company into two divisions the commercial lines division led by Rick Patina and the personal lines division led by Henry Rodrigues. This should result in a greater focus in the company on each of the different lines of business. In July 1995 Lombard and Henry Rodrigues were selected by Canadian Information Productivity Awards, out of 20,000 entries, as the Information Innovator of the Year. Independently audited, the judges felt that Henry and Lombard had "revolutionized the personal lines business with a productivity edge of up to 10:1 versus the competition". As a low cost operator in the personal lines business, this could result in significantly more business at combined ratios of less than 100%. Byron and Henry are proceeding with care!

In 1995 Lombard had gross premiums written of $510 million, up 4% from 1994. After reinsurance, Lombard had net premiums written of $444 million. The company maintains a quota share treaty with a related Bermuda company (CRC (Bermuda)). Approximately $92 million of net premiums written flows to CRC (Bermuda) and the remaining $352 million remains with Lombard. Net income after taxes (including CRC (Bermuda)) amounted to $42 million in 1995. Late in the year, as per our agreement with Continental U.S., Byron changed Continental's name to Lombard. Because of dropping interest rates, we recouped the $14 million by which Lombard's investments were written down in November 1994 because of mark-to-market purchase accounting. The prospects for Lombard look very good for a combined ratio of less than 100% in 1996.

Federated, under John Paisley's leadership, had another very good year at the property and casualty company with a combined ratio of 100.1% (102.1% including the life operations). Gross premiums increased by 18% to $55 million while net premiums written increased 19% to $47.2 million. Federated's customer retention rate in 1995 was 95% and with its specialty focus, it continues to be the leader in the farm equipment, tire dealers, plumbing and heating contractors and independent petroleum distributors markets. In 1995 Federated earned $6.9 million after taxes, about 23% less than the $9.0 million earned in 1994 because of lower investment income.

Under Mark Ram's leadership, Markel had a spectacular turnaround in 1995. After three years of combined ratios of 115%, Mark, in just a year and a half, has turned Markel around with a combined ratio of 101.9%. This, with more conservative reserving! Shows you why management skills get magnified in the insurance business both ways!! More importantly, Mark and his team are building Markel, brick-by-brick, for sustained long term success. I think it is fair to say, Markel has not been in better shape since its founding in 1951, certainly since we purchased it in 1985.

Markel's net premiums written in 1995 were $80 million versus $56 million in 1994. Net income after taxes in 1995 was $9.7 million.

Ranger had a very poor year in 1995. Prior to indemnification, Ranger had an unbelievable combined ratio of 138.0% mainly because of a very significant strengthening of case reserves. During the year, we found out that case reserving at Ranger was not adequate. After the remaining indemnification of US$11.5 million (total US$20 million indemnification secured by real estate obtained at purchase) and an additional US$14 million indemnification provided by Fairfax (backed mainly by the $14 million recouped from Lombard as mentioned earlier), Ranger reported a combined ratio of 118.1%. This was very disappointing to us and you have every right to question our judgment again!! However, before you sell your stock you may want to consider the following points on Ranger:

1) We think we have licked the reserving problem and perhaps gone too far. We'll know by this time next year.
2) In spite of this reserving hit, Ranger earned $18 million after tax in 1995 after the indemnifications discussed above because of capital gains (mainly stocks) of $34 million and interest and dividend income of $17 million.
3) Pete Wallner took over as President in May 1995. We feel comfortable that Pete will return Ranger to its traditional strengths in its core lines and that 1995 will not be repeated.
4) Pete has discontinued the poor performing lines, reduced overhead and focused on underwriting profitability by increasing retentions in our core lines like propane and petroleum distributors.
5) In spite of its reserving hit, Ranger ended the year with the highest statutory capital position it has ever had and A.M. Best continues to rate it an A (excellent).

All in all, Pete and the management team at Ranger have come through a gruelling year, but with continued strong support from Fairfax we expect 1996 to be a much improved year and on the way to sustained underwriting profitability.

Wentworth, our Barbados company, had an excellent year in 1995. Because of the absence of catastrophes, Wentworth had a combined ratio of 62% on net premiums earned of $16 million. Wentworth earned $8.0 million in 1995 versus $0.5 million in 1994.

Early in 1995 Kris Datt joined us to begin an international property reinsurance division in New York. Kris has had an excellent long term track record of underwriting profitability and we look forward to his group's contribution to Fairfax.

Our insurance companies (with the exception of Lombard) continue to have low operating leverage (net premiums written to common shareholders' equity) as shown on page **XX**.

Lombard's leverage has dropped considerably in 1995. We have the capacity to increase our premiums significantly but there are no signs that we will want to do it soon. The insurance downcycle began in 1988 and continues unabated even though there are many constructive changes taking place in the industry.

You have no doubt read about Lloyd's and the problems that that institution is going through. You will be happy to know that our exposure to Lloyd's is very minimal. We are mindful of our reinsurance recoverables and deal only with the most financially sound reinsurers.

Our reserves continue to be certified at the individual insurance company level by Joe Cheng for Commonwealth, Ron Miller for Federated, Lombard and Markel, and Coopers & Lybrand for Ranger. They are then reviewed on a consolidated basis and certified by Coopers & Lybrand. All of this is in addition to the extensive monitoring and analysis done by our actuary at Fairfax, Sam Chan. Sam's and our goal at Fairfax is to ensure that the reserve "past" does not hurt us in the future but helps us, i.e. it is a very important policy of ours to ensure that we have redundancies each year in each of our insurance companies. In spite of this focus, we have had Ranger! So you can see it is not easy but we are persevering.

We provide extensive disclosure on our total claims reserves beginning on page **XX** which will help you appraise our past reserving accuracy. As discussed in the MD&A, our Canadian insurance companies, excluding Lombard, had redundancies; including Lombard, after its $7.0 million indemnification they had a redundancy of $2.9 million. As discussed earlier, Ranger had a very poor year, resulting in a net US$4.1 million deficiency (or US$38.1 million before indemnifications). While we are not pleased with our reserving surprise at Ranger, rest assured we will not tolerate lax reserving practices. All in all, over the past ten years, our reserving has been good no room for complacency though!

Claims adjusting

Ken Polley and Lindsey Morden came through for us in 1995. After many years of grinding it out in the pits, Ken and his management team achieved record earnings in 1995. In spite of flat revenue of $155 million (versus $156 million in 1994), Lindsey Morden earned a record $8.1 million before taxes and $4.1 million after taxes an 11% return on average shareholders' equity. We continue to feel that Ken, with the support of Don Cain, Don Smith and Duncan Smith, will achieve our 20% return on equity target and make this a very attractive investment for its shareholders (including us).

You will note that during 1995 Morden & Helwig changed its name to Lindsey Morden to better reflect its extensive operations in the U.S.

Lindsey Morden's balance sheet improved in 1995 due to the record earnings. Its debt to equity ratio improved to 0.45:1 from 0:55:1 in 1994. We are breathing a little easier on the goodwill shown on the company's balance sheet!!

During the year Lindsey Morden's subordinated convertible debenture was refinanced for an additional five years at fair terms for the company. The coupon on the debenture was reduced to 8% from 10% and the conversion price to $7.50 per share from $11.00. Lindsey Morden could not have refinanced its convertible debenture at more favourable terms in the marketplace. Fairfax, as the holder of this debenture, plans to convert it into subordinate voting shares before the maturity date (assuming this is justified by the share price).

For further information on Lindsey Morden, please read its annual report available by phoning Duncan Smith at (416) 362-6762.

Investment management

1995 was an excellent year on an absolute and relative basis for U.S. equities and bonds. This was not the case for Canadian equities. However, as shown below, on a long term basis the partners of HWIC have produced excellent results in each of the areas in which they provide investment management Canadian equities, U.S. equities, Canadian bonds and balanced funds.

Annualized rates of return (%)

Cumulative periods ended December 31, 1995

	5 years	**10 years**	**15 years**
Canadian Equities	16.9	11.2	13.5
TSE 300	10.8	8.3	8.7
U.S. Equities	34.2	19.6	19.5
S&P 500	20.4	14.6	15.8
Canadian Bonds	16.9	12.1	
SM Index	12.8	11.3	
Balanced Fund	18.4	13.4	

Source: Representative balanced fund managed by HWIC for eleven years. Equity results for an additional four years are from the organization for which the principals previously worked.

Because of the poor relative returns in 1995, HWIC did not earn any incentive fees and, in fact, had to provide each client with a 10% discount on their fees. Total fees in 1995 were $5.3 million, down 43% from $9.3 million in 1994 because there were no incentive fees in 1995. In spite of the drop in revenue, Fairfax earned a 17% pre-tax cash return in 1995 on its $14 million investment in HWIC. We should repeat again that while returns after goodwill amortization (of $1.4 million annually) will be less than those mentioned above, we think the returns we have shown are the best measure of HWIC's performance.

Financial position

As in previous reports, we feel our unaudited balance sheet with Lindsey Morden equity accounted (shown on page **XX**) is the best way to understand our financial position. We have changed the table below because our recent long term debenture issue (US$100 million at 8¼% for 20 years) resulted in a significant amount of cash in our holding company.

Here's what our year-end financial position looks like compared to the end of 1994:

		($ millions)
	1995	**1994**
Cash and short term investments	$ 70.4	$ 7.2
Short term bank debt		
Long term bank debt		60.0
Long term debentures	298.0	165.3
Total debt	298.0	225.3
Net debt	228.6	218.1
Common shareholders' equity	472.6	392.0
Net debt/equity 48%	56%	
Net debt/total capital	30%	35%

As shown, common shareholders' equity increased by $80.6 million $87.5 million from net income less $6.9 million used to purchase 85,100 shares at $81 per share. The long term debentures increased because of the US$100 million debenture issue in October 1995. Proceeds of C$133 million were used to fully repay the long term bank debt of $60 million, leaving $70 million in cash in the holding company after $3 million of net disbursements. Given our current cash position in the holding company and our plans always to have a significant cash position, we have changed our definition of debt to net debt which means total debt less cash. We think net debt to equity is a better ratio for us than the gross debt to equity ratio. Obviously, this puts our financial position in a better light and so you may properly be sceptical. When management cannot meet its targets, it usually resorts to changing the targets to meet its actual results. Having said that, we do feel this change applies to us. Our net debt to equity ratio and net debt to total capital ratio dropped significantly from 56% and 35% respectively at year-end 1994 to 48% and 30% at year-end 1995.

Also, by year-end 1995 we had increased our unused, unsecured, committed, long term bank lines to $215 million (from $105 million) from six major banks three Canadian, two U.S. and one European. As emphasized in the past, these are unused bank lines and provide us with flexibility on an emergency basis we will not use them to make an acquisition. By the way, we pay 0.25% per annum (i.e. approximately $540,000 annually) for the privilege of having these lines. A little insurance you may say!

We also have letter of credit (LOC) facilities in excess of $70 million for use in the ordinary course of our insurance businesses. As mentioned earlier in the report, Fairfax ended 1995 in the strongest financial position it has ever been in during its ten year history.

Why do we feel this way? Because of the following:

1) We have no bank debt. Our debt consists of two public debenture issues with a long term to maturity (8 years and 20 years respectively) and low interest rates (7¾% and 8¼% respectively), and a small eight year 7¾% debenture issued to a vendor. All of this debt was issued under a single trust indenture containing a covenant package that provides us with great flexibility.

2) We have unused, unsecured, committed, long term bank lines of $215 million with excellent covenants with three Canadian, two U.S. and one European bank. In addition, we have LOC facilities in excess of $70 million.

3) Our net long term debt is less than three times our expected earnings base. Also, our earnings base is well diversified between many insurance companies, Lindsey Morden and HWIC, and Canadian and U.S. streams of income.

4) Cash flow at the Fairfax (holding company) level from dividends, management fees and interest covers our expenses (administrative and interest) by about two times. Note Fairfax's parent company-only income statement on page **XX**.

5) For the first time in Fairfax's history, we have about $70 million of cash at the holding company which means we can pay our interest expenses for about three years with no dividends being taken from our regulated insurance companies.

6) As discussed in the MD&A, our insurance companies are all over-capitalized with large solvency margins in excess of mandated regulatory levels. This includes Lombard, which was not as strong last year.

7) Our foreign exchange exposure with respect to the balance sheet and future U.S dollar income (mainly Ranger) was fully hedged at year-end 1994 by our first US$100 million

debenture issue and foreign exchange contracts. With our second US$100 million debenture issue in 1995, we felt the balance had shifted the other way and our U.S. liabilities exceeded our assets. So we unwound our US$25 million foreign exchange contract at C$1.50 to US$1.00 (at a profit of $2.2 million) and are looking at partially unwinding the US$50 million foreign exchange contract at C$1.37 to US$1.00 during 1996. The additional foreign exchange contracts mentioned in note 9 to the financial statements hedge U.S. portfolio investments in Canadian insurance subsidiaries.

Long term shareholders should note that the reasons discussed above put Fairfax in its strongest financial position ever even though in the early years we had little or no debt.

Investments

1995 was an excellent year for stock and bond markets particularly for the U.S. stock market and bonds. While our results relative to the indices were not very good in 1995, it was a record year for realized gains. The change in unrealized gains or losses is shown below:

($ millions)

	1995	**1994**
Bonds	21.7	(17.5)
Preferred stocks	5.7	(1.4)
Common stocks	(12.9)	(12.1)
	14.5	(31.0)

Declining interest rates and rising stock markets resulted in a $31.0 million unrealized loss being transformed into a $14.5 million unrealized gain. This was after a record $72 million in realized gains in 1995. To put the realized gains in perspective, it took us nine years to achieve cumulative realized gains of $83 million we achieved 87% of that in the tenth year alone!! The $72 million in gains consisted of $62 million realized from stock gains and $10 million from bonds. The $62 million realized from stocks is about a 17% return on an average common stock portfolio of approximately $357 million about 7% above the 10% interest income we could have obtained if it was all invested in bonds.

After a year like 1995, some of you probably think that we have scraped the bottom of the barrel as far as realized gains are concerned and perhaps used it all to achieve our 20% objective in 1995. While we always look at the long term, we remain sceptical of managements who forever are promising good things in the distant future but don't deliver in the present. After all, many of our long term decisions in the past should blossom in the present if they were good decisions! So while we balance the present with the long term, rest assured that we expect to make significant realized gains on the approximately $390 million that we had invested in U.S. and

Canadian stocks at the end of 1995 though the timing of these returns is entirely unpredictable.

Our aggregate provisions for losses on investments as at December 31, 1995 of $9 million increased by $2 million from December 31, 1994. We feel these provisions are adequate to provide against unexpected events taking place in the future.

The table on page **XX** shows the returns on our investment portfolios. Investment income (interest and dividends) has increased dramatically because of the Lombard investment portfolio. After tax investment income per share has increased to $8.25 from $4.85 in 1994. Since the 45¢ per share generated in 1985, after tax investment income per share has compounded at 34% annually.
Gross realized gains totalled $80.2 million. After realized losses of $6.3 million and increased provisions of $2.0 million, net realized gains were $71.9 million. The major contributors to realized gains were Magma Copper ($9.7 million), Loews ($5.8 million), Repap ($5.3 million), Bristol Myers ($3.3 million), AIG ($3.0 million), Berkley ($2.2 million), Rainy River ($1.7 million), Brascan ($1.7 million), Security Capital ($1.6 million), Noranda ($1.6 million), Stelco ($1.5 million), Canadian Tire ($1.2 million), Toronto-Dominion Bank ($1.0 million) and Alcan ($1.0 million).

At the end of 1995 we had approximately $390 million or $44 per share invested in common shares. Canadian common shares amounted to approximately $270 million while U.S. common shares were approximately $120 million. Of this amount, $154 million was invested in financial services companies, $62 million in industrial products companies and $39 million in natural resource companies. With the Dow Jones making record highs, we are reminded again of Ben Graham's statement from "The Intelligent Investor" that we quoted to you in our 1987 Annual Report after the crash in October. Ben said,

> "The investor with a portfolio of sound stocks should expect their prices to fluctuate and should neither be concerned by sizeable declines nor become excited by sizeable advances. He should always remember that market quotations are there for his convenience, either to be taken advantage of or to be ignored. He should never buy a stock because it has gone up or sell because it has gone down. He would not be far wrong if this motto read more simply: 'Never buy a stock immediately after a substantial rise or sell one immediately after a substantial drop.' "

While we are finding it difficult to identify good long term values in the U.S., in Canada we continue to find them quite abundantly. The Canadian market has lagged the U.S. market very significantly in the last ten years but we expect it to catch up in the future. We hope this means the Canadian market will go up to bridge the difference as opposed to the opposite!!

Our "nuclear bomb" testing on insurance regulatory capital of a simultaneous decline of 50% in our common stock holdings, 30% in our preferred stock holdings and 20% in our bond holdings resulted in the purchase of a "put" at Lombard. We purchased a two year put on the TSE 300 in February 1995, off 20% from the prevailing level, to hedge the $70 million in Canadian stocks that we owned in Lombard. We paid $1 million for this insurance which resulted in a very significant reduction in the additional capital which would be required for Lombard if the "nuclear bomb" exploded. While we don't expect the "nuclear bomb" scenario to materialize, all our insurance companies are well protected if it does.

Chandran Ratnaswami joined us late in 1995. Paul Fink and Chandran are reviewing international insurance and common stock investments for us. This may be our acorn for a future oak tree!!

While we have almost eliminated our very small past investments in real estate, in 1995 we purchased a 45% interest in two office buildings in downtown Toronto. Why the change of heart on real estate? Basically, John, Rick and I could not resist the allure of first class office buildings in prime downtown locations in our home town being offered on very reasonable terms. We think we bought them at good prices, certainly well down from what they were selling at in 1988/89 but only time will tell if the returns work out well!

Miscellaneous

In 1995 Fairfax and its subsidiaries donated approximately $953,000 (1% of pre-tax income) to a variety of charities across North America.

We remind you to review page **XX** which is an unaudited, unconsolidated balance sheet on an equity accounted basis showing you where your money is invested. As you can see, we have $653.7 million invested in our insurance companies, $28.1 million in Lindsey Morden, $11 million in HWIC and over $70 million in cash. Our insurance companies and Lindsey Morden are shown at their underlying book values. Our insurance companies continue to be very conservatively valued.

You know about our dividend policy. Last year, though, we indirectly gave you a $0.77 per share dividend by retiring 85,100 shares at $81 per share for a total cost of $6.9 million. If we had distributed the $6.9 million to you, you would have received approximately $0.77 per share on the 8.9 million shares outstanding. We think this continues to be the most tax effective way of distributing excess capital. In our 1992 Annual Report, we said that we would consider buying back our shares at close to book value as long as it was within our financial capability.

As demonstrated by our purchases in 1995, we are a little less sensitive about the price we pay for our shares as long as our long term prospects for a 20% return remain intact.

We decided to list the risks that we face in the section on Issues and Risks on page **XX**. You should read them carefully because they can be significant in the short term. However, in the long term, with the good people we have at Fairfax and our subsidiaries and our way of doing business, our flexible corporate structure, significant sustainable investment income and our share of good fortune, we expect to continue to earn a return on shareholders' equity in excess of 20% by running Fairfax for the benefit of customers, employees and shareholders.

In late 1994 and in 1995 two of the founders of Markel Financial, our predecessor company, passed away. We record with much sadness the deaths of Stanley and Milton Markel, the fathers of Steven and Tony Markel respectively. On a happier note, one of our directors, Winslow Bennett, celebrated his 70th birthday in 1995. Winslow was one of the founding shareholders of Sixty Two and continues to support us wholeheartedly.

We had an excellent annual meeting last year at the old Toronto Stock Exchange building on Bay Street excellent because many of you came and asked questions that benefitted all shareholders. This year our annual meeting will be held at the same place again (the Design Exchange, 234 Bay Street, Toronto) at 4:30 p.m on April 17, 1996. We hope to see as many of you there as possible.

Again, on your behalf, I would like to thank the Board and the management and employees of all our companies for another great year.

March 1, 1996

V. Prem Watsa

Chairman and Chief Executive Officer

Consolidated Financial Statements

for the years ended December 31, 1995 and 1994

Consolidated Balance Sheets
as at December 31, 1995 and 1994

	1995 ($000)	1994 ($000)
Assets		
Cash and short term investments	70,354	7,242
Accounts receivable	400,153	365,430
Claims in process	15,390	14,842
Income taxes refundable	18,530	9,845
Prepaid expenses	12,575	10,189
	517,002	407,548
Portfolio investments		
Subsidiary cash and short term investments	256,677	263,784
Bonds (market value $821,244; 1994 $775,564)	799,507	793,113
Preferred stocks (market value $160,298; 1994 $158,053)	154,646	159,388
Common stocks (market value $373,990; 1994 $314,484)	386,907	326,568
Total (market value $1,612,209; 1994 $1,511,885)	1,597,737	1,542,853
Deferred premium acquisition costs	84,859	82,656
Deferred income taxes	34,163	39,908
Capital assets (note 2)	33,763	29,832
Goodwill	46,449	51,388
Other assets	18,878	19,226
	2,332,851	2,173,411

Signed on behalf of the Board

Director

Director

	1995	**1994**
	($000)	*($000)*
Liabilities		
Bank indebtedness (note 3)	7,621	8,875
Accounts payable and accrued liabilities	168,404	168,245
Premium deposits	10,929	7,541
	186,954	184,661
Provision for claims	912,655	921,674
Unearned premiums	431,533	417,318
Long term debt (note 4)	310,236	240,494
	1,654,424	1,579,486
Non-controlling interest	18,919	17,315
Shareholders' Equity		
Capital stock (note 5)	225,295	227,803
Retained earnings	247,259	164,146
	472,554	391,949
	2,332,851	2,173,411

Consolidated Statements of Earnings
for the years ended December 31, 1995 and 1994

	1995 ($000)	1994 ($000)
Revenue		
Premiums earned	829,340	400,559
Claims fees	154,914	156,093
Interest and dividends	89,354	58,219
Realized gains on investments	71,912	20,026
	1,145,520	634,897
Expenses		
Losses on claims	614,059	296,641
Operating expenses	304,969	240,695
Interest expense	21,171	13,195
Commissions, net	109,404	38,407
	1,049,603	588,938
Earnings before income taxes	95,917	45,959
Provision for income taxes (note 7)	6,455	7,347
Earnings from operations	89,462	38,612
Non-controlling interest	(1,965)	(507)
Net earnings	87,497	38,105
Net earnings per share (note 11)	$9.79	$4.66

Consolidated Statements of Retained Earnings
for the years ended December 31, 1995 and 1994

	1995 ($000)	1994 ($000)
Retained earnings beginning of year	164,146	126,041
Net earnings for the year	87,497	38,105
Excess over stated value of shares purchased for cancellation (note 5)	(4,384)	—
Retained earnings end of year	247,259	164,146

Consolidated Statements of Changes in Cash Resources

for the years ended December 31, 1995 and 1994

	1995	**1994**
	($000)	*($000)*
Operating activities		
Earnings from operations	89,462	38,612
Amortization	12,699	9,429
Deferred income taxes	(805)	4,219
Gains on investments	(71,912)	(20,026)
	29,444	32,234
Increase (decrease) in provision for claims	(9,019)	15,825
Increase in unearned premiums	14,215	15,048
Decrease in cash funds resulting from changes in other operating working capital items	(36,246)	(46,619)
Cash resources provided by (used in) operating activities	(1,606)	16,488
Investing activities		
Investments net sales (purchases)	9,576	(139,151)
Purchase of capital assets	(13,200)	(5,118)
Purchase of subsidiary, net of cash acquired	—	(54,956)
	(3,624)	(199,225)
Financing activities		
Net capital stock transactions (note 5)	(6,892)	74,365
Increase in long term debt, net (note 4)	69,742	93,744
Change in non-controlling interest	(361)	(638)
	62,489	167,471
Increase (decrease) in cash resources	57,259	(15,266)
Cash resources beginning of year	262,151	277,417
Cash resources end of year	319,410	262,151

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

Notes To Consolidated Financial Statements
for the years ended December 31, 1995 and 1994
(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 is engaged in the insurance of property, casualty and life risks, investment management 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., Ranger Insurance Company, Lombard General Insurance Company of Canada (formerly The Continental Insurance Company of Canada Inc.), CRC (Bermuda) Reinsurance Limited and Hamblin Watsa Investment Counsel Ltd., all 100% owned; and Lindsey Morden Group Inc. (formerly Morden & Helwig Group Inc.), 57% equity and 92% 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. Such writedowns are reflected in realized gains (losses) on investments. At December 31, 1995 the aggregate provision for losses on investments was $8.9 million (1994 $6.9 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 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.

The operations of the company's subsidiaries in the United States are self-sustaining. As a result, the assets and liabilities of these subsidiaries are translated at the year-end rates of exchange. Revenue and expenses are translated at the average rate of exchange for the years. The unrealized gains and losses, if material, which result from translation would be deferred and included in shareholders' equity under a caption "currency translation adjustment".

The company enters into foreign currency contracts from time to time to hedge the foreign currency exposure related to its net investments in self-sustaining foreign operations. Such contracts are translated at the year-end rates of exchange and a corresponding adjustment, if material, would be included in the currency translation adjustment account in shareholders' equity.

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 their estimated useful life which ranges from ten years for Hamblin Watsa Investment Counsel Ltd. and Ranger Insurance Company to 40 years for Lindsey Morden Group Inc. The company assesses the continuing value of goodwill based on the underlying cash flows and operating results of the subsidiaries.

2. **Capital Assets**

	1995 *($000)*	**1994** *($000)*
Land and buildings	5,302	5,360
Furniture and equipment	55,924	45,197
Leasehold improvements	9,582	4,147
Automobiles under capital lease	968	1,044
	71,776	55,748
Accumulated amortization	38,013	25,916
	33,763	29,832

Amortization for the year was $9,269 (1994 $5,755).

3. Bank Indebtedness

Bank indebtedness is $7,621 (1994 $8,875) for which a general assignment of accounts receivable and claims in process of subsidiaries of Lindsey Morden Group Inc. have been pledged as security. Interest expense on bank indebtedness amounted to $1,200 (1994 $1,071).

4. Long Term Debt

The long term debt at December 31 consists of the following balances:

	1995 ($000)	1994 ($000)
Fairfax unsecured senior notes of US$100 million at 7.75% due December 15, 2003	136,520	140,280
Fairfax unsecured senior notes of US$100 million at 8.25% due October 1, 2015	136,520	—
Fairfax unsecured senior note at 7.75% due December 15, 2003	25,000	25,000
Fairfax unsecured bank term credits due December 30, 1999 at short term BA rates of 6.10% per annum at December 31, 1994	—	60,000
Long term debt of Lindsey Morden Group Inc. at an average annual rate of 8.01% during 1995 (1994 7.25%)	12,196	15,214
	310,236	240,494

Interest expense on long term debt amounted to $19,971 (1994 $12,124).

Principal repayments on these loans are due as follows:

	($000)
1996	1,672
1997	12,077
1998	119
1999	
2000	
Thereafter	298,040
	311,908
Less: current portion	1,672
	310,236

5. 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

	1995		1994	
	number	*($000)*	*number*	*($000)*
Subordinate voting shares	8,120,658	239,317	8,205,758	241,825
Multiple voting shares	1,548,000	5,000	1,548,000	5,000
	9,668,658	244,317	9,753,758	246,825
Interest in shares held through ownership interest in shareholder	(799,230)	(19,022)	(799,230)	(19,022)
Net effectively outstanding	8,869,428	225,295	8,954,528	227,803

On October 12, 1994 the company issued 1,000,000 subordinate voting shares at $76 per share, for net proceeds of $74,365.

In 1995, under the terms of a normal course issuer bid approved by The Toronto Stock Exchange, the company purchased and cancelled 85,100 subordinate voting shares for an aggregate cost of $6,892, of which $4,384 was charged to retained earnings.

6. Reinsurance

The company follows the policy of underwriting and reinsuring contracts of insurance, which generally limits the liability of the individual insurance companies to a maximum amount on any one loss of $500 to $2,500, varying by line of business. 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, 1995 provision for claims reflects recoveries from reinsurers of $469,565 (1994 $408,566). During the year the company ceded $349,932 (1994 $188,740) of premium income and $318,789 (1994 $227,929) of claims incurred.

7. 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 in the following table:

	1995 ($000)	1994 ($000)
Provision for taxes at statutory marginal income tax rate	41,583	21,798
Non-taxable investment income	(8,689)	(9,743)
Recovery of claims on non-taxable purchase price adjustment	–	(3,732)
Income earned outside Canada	(3,451)	(246)
Utilization of prior years' losses and other	(22,988)	(730)
Provision for income taxes	6,455	7,347

As at December 31, 1995 tax losses were insignificant.

8. Statutory Requirements Insurance Subsidiaries

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

9. **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 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 $11,135 (1994 $8,728) for which 399,092 (1994 478,292) subordinate voting shares of the company with a year-end market value of $39,111 (1994 $32,045) have been pledged as security.

At December 31, 1995 the company had net foreign currency contracts outstanding to sell the equivalent of US$80 million, primarily to hedge future earnings from U.S. subsidiaries and U.S. portfolio investments in Canadian subsidiaries.

10. Operating Leases

Aggregate future commitments at December 31, 1995 under operating leases relating to premises, automobiles and equipment for various terms up to ten years are as follows:

	($000)
1996	30,200
1997	24,500
1998	19,300
1999	13,800
2000	12,100
Thereafter	31,100
	131,000

11. Earnings per Share

Fully diluted and basic earnings per share are the same in 1995 and 1994. Basic earnings per share are $9.79 for 1995 and $4.66 for 1994. The weighted average number of shares for 1995 was 8,933,098 (1994 8,173,706).

12. Acquisitions

Effective November 30, 1994 the company purchased Lombard General Insurance Company of Canada (then The Continental Insurance Company of Canada) of Toronto, Ontario. The purchase price of $155 million was paid $130 million cash and a $25 million 7.75% note due December 15, 2003. At November 30, 1994 Lombard had $904 million in total assets and $741 million in total liabilities, at fair values. The vendor has agreed to indemnify Fairfax, to a maximum of $40 million, for any inadequacy in Lombard's provision for claims as at December 31, 1993, any of Lombard's reinsurance relating to the period up to December 31, 1993 which subsequently becomes unrecoverable, and any defaults under the purchase agreement. Certain of the vendor's marketable bonds have been pledged as security for this indemnity. The vendor may be entitled to additional consideration of up to $10 million based on future years' results and 50% of any redundancy in Lombard's provision for claims as at December 31, 1993.

Lombard is engaged in the property and casualty insurance business in Canada. Net premiums earned for the year ended December 31, 1994 amounted to $390 million.

13. Segmented Information

The company is a financial services holding company which through its subsidiaries is engaged in the insurance of property, casualty and life risks, investment management (included in "Corporate") 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**	
	1995	**1994**	**1995**	**1994**	**1995**	**1994**	**1995**	**1994**
	($000)	*($000)*	*($000)*	*($000)*	*($000)*	*($000)*	*($000)*	*($000)*
Revenue	985,916	478,995	154,914	156,093	4,690	(151)	1,145,520	634,897
Earnings before income taxes	102,920	59,006	8,083	3,036	(15,086)	(16,083)	95,917	45,959
Identifiable assets	2,155,779	2,041,614	96,836	95,908	80,236	35,889	2,332,851	2,173,411
Amortization	7,691	4,357	3,618	3,682	1,390	1,390	12,699	9,429
Interest expense			2,875	2,822	18,296	10,373	21,171	13,195

(b) Geographic segments

	Canada		**United States**		**Total**	
	1995	**1994**	**1995**	**1994**	**1995**	**1994**
	($000)	*($000)*	*($000)*	*($000)*	*($000)*	*($000)*
Revenue	766,783	269,877	378,737	365,020	1,145,520	634,897
Earnings before income taxes	54,640	26,576	41,277	19,383	95,917	45,959
Identifiable assets	1,591,038	1,437,151	741,813	736,260	2,332,851	2,173,411
Amortization	10,552	7,348	2,147	2,081	12,699	9,429
Interest expense	20,415	12,408	756	787	21,171	13,195

CRC (Bermuda) Reinsurance is included in the Canadian segment and Wentworth Insurance is included in the United States segment.

14. Subsequent Event

On February 21, 1996 the company announced that it had agreed to purchase Skandia America Reinsurance Corporation for about US$230 million cash. At December 31, 1995 Skandia had US$1.3 billion in total assets and shareholders' equity of US$344 million. Skandia is engaged in the property and casualty reinsurance business in the United States and Canada, and gross premiums written in 1995 were US$205 million. Completion of the purchase is subject to various closing conditions including applicable regulatory approvals.

February 7, 1996 (February 21, 1996 as to note 14)

Auditors' Report to the Shareholders

We have audited the consolidated balance sheets of Fairfax Financial Holdings Limited as at December 31, 1995 and 1994 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, 1995 and 1994 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 7, 1996

Valuation Actuary's Report

Coopers & Lybrand has valued the policy liabilities of the subsidiary insurance companies of Fairfax Financial Holdings Limited in its consolidated balance sheet at December 31, 1995 and their change as reflected in its consolidated statement of earnings for the year then ended in accordance with accepted actuarial practice except as described in the following paragraph.

Under accepted actuarial practice, the valuation of policy liabilities reflects the time value of money. Pursuant to the authority granted by the Insurance Companies Act, the Superintendent of Financial Institutions has directed that the valuation of some policy liabilities not reflect the time value of money. Our valuation complies with that directive.

In our opinion the valuation is appropriate, except as noted in the previous paragraph, and the consolidated financial statements fairly present its results.

Coopers & Lybrand
Richard Gauthier, FCIA, FCAS
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 Lindsey Morden 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 five years:

Revenue by Line of Business	**1995**	**1994**	**1993**	**1992**	**1991**
	($000)	*($000)*	*($000)*	*($000)*	*($000)*
Insurance	973,143	476,445	201,402	143,915	116,038
Claims adjusting	154,914	156,093	142,105	139,782	122,982
Other income	17,463	2,359	515	3,133	10,982
	1,145,520	634,897	344,022	286,830	250,002

The increase in insurance revenue in 1995 over 1994 was mainly the result of the November 30, 1994 acquisition of Lombard which resulted in higher insurance premiums and investment income. Significantly higher realized gains as well as higher premiums in Markel, Federated and Wentworth also contributed to the increase in 1995.

Claims adjusting revenue decreased slightly in 1995, largely due to the effect of the better weather and reduced earthquake-related revenue.

On a geographic basis, Canadian operations accounted for approximately 67% of Fairfax's revenue and 57% of operating profits in 1995, compared with approximately 44% of revenue and 59% of operating profits in 1994.

Canadian insurance operations accounted for approximately 65% of Fairfax's insurance premiums in 1995.

Net Earnings

Sources of net earnings with Lindsey Morden equity accounted were as follows for the past five years:

	1995	**1994**	**1993**	**1992**	**1991**
	($000)	*($000)*	*($000)*	*($000)*	*($000)*

Insurance underwriting	(40,883)	(16,880)	2,065	(16,883)	5,320
Interest and dividends	86,274	53,742	23,006	22,786	25,360
Gain on sale of F-M Acquisition	_____	_____	_____	_____	13,636
Insurance earnings before realized gains	45,391	36,862	25,071	5,903	44,316
Claims adjusting (Fairfax portion)	2,098	532	395	282	117
Interest expense	(19,086)	(10,426)	(4,228)	(5,552)	(6,911)
Goodwill amortization	(1,390)	(1,392)	(1,392)	(232)	
Corporate overhead and other	(8,993)	(2,147)	(2,862)	2,078	(2,819)
Realized gains	71,912	20,026	27,822	3,400	(4,512)
Pre-tax income	89,932	43,455	44,806	5,879	30,191
Less: taxes	2,435	5,350	11,466	(4,166)	7,676
Net earnings	87,497	38,105	33,340	10,045	22,515

Net earnings in 1995 were $87.5 million, an increase of $49.4 million or 130% from 1994 net earnings of $38.1 million.

The major changes which affected net earnings were:

- Insurance earnings before realized gains increased by $8.5 million from 1994 due to increased interest and dividend income, partially offset by higher underwriting losses
- Net realized gains increased in 1995 to $71.9 million from $20.0 million in 1994
- Interest increased in 1995 due to higher interest expenses from the debt related to the purchase of Lombard
- Corporate overhead and other increased mainly because of one time expenses associated with the debt issue, the start-up of our reinsurance division in New York, reduced income from Hamblin Watsa and other expenses
- The provision for income taxes was lower in 1995 due to the utilization of available losses and loss carry forwards, a greater amount of tax-free Canadian dividend income and higher income from lower taxed non-North American operations.

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 the past eleven years:

	NET PREMIUMS		RATIOS		
	Written *($000)*	**Earned** *($000)*	**Loss** *(%)*	**Expense** *(%)*	**Combined** *(%)*
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
1993	163,508	150,844	73	26	99
1994	411,570	400,559	74	30	104
1995	864,589	829,340	74	31	105

In 1995 the combined ratio increased due to poor results at Ranger. Since current management took over in September 1985 the company has had combined ratios of less than 100% in five of the ten years and greater than 100% in the remaining five years.

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

		1995 *($000)*	**1994** *($000)*	**1993** *($000)*	**1992** *($000)*	**1991** *($000)*
Markel	Written	79,683	55,937	44,896	38,422	23,159
	Earned	56,976	52,149	43,749	33,760	20,594
Federated	Written	57,549	50,396	41,629	38,923	37,249
	Earned	54,297	47,376	40,436	38,776	38,838
Commonwealth	Written	87,875	90,403	71,181	51,319	33,042
	Earned	86,962	86,520	61,855	46,318	31,075
Ranger	Written	180,253	175,410			
	Earned	173,937	179,345			
Lombard	Written	351,592	30,727			
	Earned	352,082	26,869			
CRC (Bermuda)	Written	92,270				
	Earned	89,252				
Wentworth and other	Written	15,367	8,697	5,802		
	Earned	15,834	8,300	4,804		
Totals	Written	864,589	411,570	163,508	128,664	93,450
	Earned	829,340	400,559	150,844	118,854	90,507

Net premiums written increased at Markel and Federated in 1995 due to price increases and additional accounts written. Ranger and Lombard were included in Fairfax's income statements for the first time in 1994 for a year and for one month respectively. CRC (Bermuda)'s premiums written originate mainly from a quota share treaty with Lombard.

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

	1995 *($000)*	**1994** *($000)*	**1993** *($000)*	**1992** *($000)*	**1991** *($000)*
Markel	(1,088)	(7,965)	(5,088)	(5,000)	4,940
Federated	(1,120)	257	(1,320)	(1,294)	951
Commonwealth	9,104	1,867	5,126	(9,959)	196
Ranger	(31,524)	(15,061)			
Lombard	(30,915)	(143)			
CRC (Bermuda)	6,635				
Wentworth and other	8,025	4,165	3,347	(630)	(767)
Totals	(40,883)	(16,880)	2,065	(16,883)	5,320

As shown, in 1995 the most significant underwriting loss by far (in relationship to premiums earned) was incurred at Ranger, followed by Lombard. Lombard's underwriting loss should be considered together with CRC (Bermuda)'s underwriting profit. Excluding Ranger, Fairfax had an underwriting loss of $9.4 million or a combined ratio of 101%. As discussed in the Chairman's section, management does not expect Ranger's loss to be repeated. In 1994 the underwriting losses at Ranger and Markel more than offset the underwriting profits at Commonwealth and Federated. The Wentworth and other underwriting profit includes a $4 million consolidation adjustment in 1994 related to a previous acquisition and miscellaneous adjustments in 1991 and 1992. The underwriting loss in 1992 at Commonwealth was due to Hurricane Andrew.

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 following table presents a reconciliation of the provision for claims and loss adjustment expense (LAE) by company for the past five years. As shown in the table, the sum of the provision for claims for each of Fairfax's insurance subsidiaries is $912.7 million as at December 31, 1995 the amount shown as "Provision for claims" on Fairfax's balance sheet on page **XX**.

Reconciliation of Provision for Claims and LAE as at December 31

	1995	**1994**	**1993**	**1992**	**1991**
	($000)	*($000)*	*($000)*	*($000)*	*($000)*
Commonwealth, Federated and Markel	219,406	211,313	185,010	179,588	168,394
Lombard	326,331	311,546			
Ranger	169,017	217,251	235,525		
Federated Life	22,214	22,975	22,825	22,794	21,337
CRC (Bermuda)	163,592	150,930			
Wentworth	12,095	7,659	1,486	6,381	5,196
Other				53	7,193
Total provision for claims and LAE	912,655	921,674	444,846	208,816	202,120

The four tables that follow show the reconciliation and the reserve development of the insurance companies' provision for claims. In order to avoid the distortions caused by foreign exchange fluctuations, separate tables are provided for the Canadian and U.S. subsidiaries of Fairfax. CRC (Bermuda) and Wentworth are included in the Canadian and U.S. operations respectively.

The following table shows for Fairfax's Canadian subsidiaries the provision for claims liability for unpaid losses and LAE as originally estimated for the years 1991 through 1995, 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 Provision for Claims

Canadian Subsidiaries (C$)

	1995	**1994**	**1993**	**1992**	**1991**
	($000)	*($000)*	*($000)*	*($000)*	*($000)*
Provision for claims and LAE at January 1 for Commonwealth, Federated and Markel	211,313	185,010	179,588	168,394	192,372
Reserves of Lombard and CRC (Bermuda) purchased November 30, 1994	462,476				
Incurred losses on claims and LAE					
Provision for current accident year's claims	456,967	139,671	102,582	94,177	63,163
Increase (decrease) in provision for prior accident years' claims	4,149	2,809	360	(393)	(17,234)
Total incurred losses on claims and LAE	461,116	142,480	102,942	93,784	45,929
Payments for losses and LAE					
Payments on current accident year's claims	(205,766)	(53,222)	(40,696)	(34,540)	(25,852)
Payments on prior accident years' claims	(233,811)	(62,955)	(56,824)	(48,050)	(44,055)
Total payments for losses and LAE	(439,577)	(116,177)	(97,520)	(82,590)	(69,907)
Provision for claims and LAE at December 31	695,328	211,313	185,010	179,588	168,394

The company strives to establish adequate provisions at the original valuation date. While the company hopes favourable development will result from the past, in 1993 and 1994 there was unfavourable development. The unfavourable development in 1995 was offset by reserve indemnification for a net redundancy of $2.9 million (shown in the table below). The company will always be subject to upward or downward development in the future.

The following table shows for Fairfax's Canadian subsidiaries the original provision for claims reserves including 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 from the respective years in which they were originally acquired:

Subsidiary	**Year Acquired**
Markel Insurance Company of Canada	1985
Federated Insurance Company of Canada	1990
Commonwealth Insurance Company	1990
Lombard General Insurance Company of Canada	1994
CRC (Bermuda) Reinsurance Limited	1994

Provision for Canadian Subsidiaries' Claims Reserve Development
(including Commonwealth, CRC (Bermuda), Federated, Lombard and Markel)

As at December 31	**1986 and prior** *($000)*	**1987** *($000)*	**1988** *($000)*	**1989** *($000)*	**1990** *($000)*	**1991** *($000)*	**1992** *($000)*	**1993** *($000)*	**1994** *($000)*	**1995** *($000)*
Provision for claims including LAE	39,522	59,400	71,964	79,357	192,372	168,394	179,588	185,010	673,789	695,328
Cumulative payments as of:										
One year later	30,233	18,752	21,015	25,194	44,055	48,050	56,824	62,955	233,811	
Two years later	38,906	27,154	33,196	35,440	76,947	75,402	87,878	105,537		
Three years later	43,588	32,919	42,043	44,169	98,149	94,834	110,565			
Four years later	46,449	37,784	47,901	50,119	115,417	110,838				
Five years later	49,549	41,128	52,103	55,310	127,003					
Six years later	51,221	43,991	55,675	58,687						
Seven years later	52,891	45,654	57,855							
Eight years later	53,554	46,352								
Nine years later	54,088									
Reserves re-estimated as of:										
One year later	59,200	56,920	71,673	80,602	175,138	168,001	179,948	187,819	677,938	
Two years later	59,690	54,920	69,930	73,904	173,992	157,848	174,820	191,825		
Three years later	59,441	53,004	67,676	71,810	165,752	157,671	171,833			
Four years later	57,741	52,295	64,478	67,165	166,797	156,291				
Five years later	58,023	50,235	64,394	65,414	165,625					
Six years later	56,573	50,822	62,939	65,181						
Seven years later	57,387	49,198	63,103							
Eight years later	56,045	49,815								
Nine years later	56,619									
Favourable (unfavourable) development before indemnification	(17,097)	9,585	8,861	14,176	26,747	12,103	7,755	(6,815)	(4,149)	
Reserve indemnification								6,300	7,009	
Favourable (unfavourable) development after indemnification								(515)	2,860	

For 1994, excluding Lombard, the Canadian insurance companies had redundancies; including Lombard, they had a net deficiency of $4.1 million. However, the reserve indemnification at Lombard protected Fairfax for $7.0 million, resulting in a $2.9 million final redundancy. For 1993, after reserve indemnification at Lombard, Canadian reserves were deficient by $0.5 million.

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

The following table shows for Fairfax's U.S. subsidiaries the provision for claims liability for unpaid losses and LAE as originally estimated for the years 1993, 1994 and 1995, 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 Provision for Claims

U.S. Subsidiaries (US$)

	1995	1994	1993
	(US$000)	*(US$000)*	*(US$000)*
Provision for claims and LAE at January 1			
for Ranger and Wentworth	160,331	179,001	5,020
Reserves of Ranger purchased			
December 31, 1993			177,887
	160,331	179,001	182,907
Incurred losses on claims and LAE			
Provision for current accident year's claims	93,235	97,899	410
Increase in provision for prior accident years' claims	38,117	8,202	
Total incurred losses on claims and LAE	131,352	106,101	410
Payments for losses and LAE			
Payments on current accident year's claims	(34,394)	(39,277)	
Payments on prior accident years' claims	(90,686)	(85,494)	(4,316)
Total payments for losses and LAE	(125,080)	(124,771)	(4,316)
Provision for claims and LAE at December 31	166,603	160,331	179,001
Exchange rate	*1.3652*	*1.4028*	*1.3241*
Converted to Canadian dollars	C$ 227,446	C$ 224,910	C$ 237,011

The unfavourable reserve development of US$38.1 million in the U.S. operations in 1995 derived from adverse development mainly from periods prior to Fairfax's acquisition of Ranger for which indemnification of US$20 million is provided under the purchase agreement. In addition Fairfax has provided a US$14 million indemnification which brings the total indemnification to US$34 million. As shown below, after indemnification, the U.S. operation had a reserve deficiency of US$4.1 million and US$0.3 million for 1994 and 1993 respectively.

The following table shows for Fairfax's U.S. subsidiaries the original provision for claims reserves including 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 from the respective years in which they were originally acquired (Wentworth from January 1, 1993 as its operations were minor prior to that):

Subsidiary	
Wentworth Insurance Company Ltd.	Commenced business 1990
Ranger Insurance Company	Acquired 1993

Provision for U.S. Subsidiaries' Claims Reserve Development (including Ranger and Wentworth)

As at December 31	**1993** (US$000)	**1994** (US$000)	**1995** (US$000)
Provision for claims including LAE	179,001	160,331	166,603
Cumulative payments as of:			
One year later	85,494	90,686	
Two years later	142,398		
Reserves re-estimated as of:			
One year later	187,203	198,448	
Two years later	213,295		
Favourable (unfavourable) development before indemnification	(34,294)	(38,117)	
Reserve indemnification	34,000	34,000	
Favourable (unfavourable) development after indemnification	(294)	(4,117)	

Insurance Environment

The property and casualty insurance market experienced improved underwriting results in 1995 with combined ratios in Canada and the U.S. expected to be approximately 104.4% and 107.2% respectively, versus 108.2% and 108.4% respectively in 1994. The improvement was due mainly to a milder winter and an absence of major catastrophes in North America. However, many insurance companies continue to write insurance at inadequate prices. Significant restructuring and consolidation continues to take place in the industry. We continue to believe that over time price increases must take place to compensate for the underwriting losses combined with interest rates which are insufficient to adequately offset these losses. Currently, however, the industry continues to be very competitive.

Lombard Acquisition

Effective November 30, 1994 the company acquired Lombard General Insurance Company of Canada (then The Continental Insurance Company of Canada) for $155 million. The combined balance sheet of Lombard upon acquisition was as follows:

	($000)
Investments, including cash	684,198
Deferred premium acquisition costs	52,362
Accounts receivable	145,218
Other assets	21,983
	903,761
Provision for claims	461,003
Unearned premiums	217,993
Other liabilities	62,068
Shareholders' equity	162,697
	903,761

The purchase price of $155 million was paid $130 million in cash and the remainder by the issue of a $25 million nine year unsecured debenture. The $7.7 million excess of the shareholders' equity over the purchase price relates essentially to an unrealized loss in a predominantly government bond portfolio with an average term of approximately three years.

Lombard underwrites a complete range of commercial and personal insurance products in Canada. Lombard's net premiums written for 1994 were $373 million.

Interest and Dividend Income

The majority of interest and dividend income is earned by the insurance companies. The Commonwealth and Federated acquisitions added $130 million and $101 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. Ranger's $400 million investment portfolio acquired effective December 31, 1993, and Lombard's $684 million portfolio acquired effective November 30, 1994, are included in the following tables only as indicated.

	Average Investments at Book Value	Pre-Tax Amount	Pre-Tax Yield	After Tax Amount	After Tax Yield	Interest and Dividend Income Per Share
	($000)	*($000)*	*(%)*	*($000)*	*(%)*	*($)*
1985	29,060	2,455	8.45	1,271	4.37	0.45
1986	64,181	4,678	7.29	2,522	3.93	0.52
1987	109,825	8,042	7.32	5,499	5.01	0.77
1988	130,782	8,922	6.82	6,618	5.06	0.90
1989	135,703	11,628	8.57	8,537	6.29	1.11
1990	237,868	20,704	8.70	14,017	5.89	1.86
1991	338,461	26,051	7.70	17,731	5.24	3.02
1992	366,481	23,988	6.55	17,749	4.84	3.09
1993 *	418,207	23,251	5.56	17,994	4.30	2.92
1994 **	852,010	58,219	6.83	39,608	4.65	4.85
1995	1,608,054	89,354	5.56	73,664	4.58	8.25

* *Ranger is not included in this line.*

** *Lombard is not included in this line.*

Interest and dividend income increased in 1995 due mainly to the inclusion of Lombard's portfolio. As shown, the after-tax income yield decreased in 1995 to 4.58% as a result of lower interest rates. After-tax interest and dividend income per share has compounded at 33.8% per year since 1985.

Investments for the past eleven years are shown in the following table, the first five columns of which show them at the average of their carrying values at the beginning and end of each year, and the final two columns of which show them at year-end.

	Cash and Short Term Investments	Bonds	Preferreds	Common	Total Investments		
					Average	Year-End	Per Share
	($000)	*($000)*	*($000)*	*($000)*	*($000)*	*($000)*	*($)*
1985	10,526	15,388	732	2,414	29,060	32,728	6.55
1986	16,605	24,523	7,979	15,074	64,181	95,633	13.65
1987	28,025	26,242	16,516	39,042	109,825	124,016	16.90
1988	29,843	23,575	25,191	52,173	130,782	137,548	18.79
1989	20,623	28,528	32,212	54,340	135,703	133,858	18.30
1990	33,596	99,220	45,652	59,400	237,868	335,740	61.30
1991	60,099	140,177	75,685	62,500	338,461	341,180	62.54
1992	77,929	108,818	99,821	79,913	366,481	396,240	65.44
1993 *	102,968	90,682	118,604	105,953	418,207	848,774	106.70
1994 **	226,205	303,859	132,138	189,808	852,010	1,551,343	173.25
1995	297,989	796,310	157,017	356,738	1,608,054	1,668,656	188.14

* *Ranger is not included in the first five columns in this line.*

** *Lombard is not included in the first five columns in this line.*

Total investments per share at year-end 1994 increased significantly due to the Lombard acquisition. The increase in total investments in 1995 was due to normal growth from the insurance business as well as additional cash from the debentures issued in October 1995. Since 1985 investments per share have compounded at 40% per year.

Return on Investment Portfolio

The following table shows the performance of the investment portfolio for the past eleven 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 Value	Interest and Dividends Earned	Realized Gains (Losses) after Provisions	Change in Unrealized Gains (Losses)	Total Return on Average Investments	
	($000)	*($000)*	*($000)*	*($000)*	*($000)*	*(%)*
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
1993 *	418,207	23,251	27,822	28,792	79,865	19
1994 **	852,010	58,219	20,026	(42,407)	35,838	4
1995	1,608,054	89,354	71,912	45,438	206,704	13

* *Ranger is not included in this line.*

** *Lombard is not included in this line.*

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 has no predictive value and variations in amount from period to period have no practical analytical value. At December 31, 1995 the aggregate provision for losses on investments was $8.9 million (1994 $6.9 million). At December 31, 1995 the Fairfax investment portfolio had an unrealized gain of $14.5 million compared to an unrealized loss at December 31, 1994 of $31.0 million.

The company has a long term value-oriented investment philosophy. It continues to expect fluctuations in the stock market.

Capital Resources

At December 31, 1995 total capital, comprising shareholders' equity and non-controlling (minority) interest, was $491.2 million, compared to $409.2 million at December 31, 1994.

The following table shows the level of capital as at December 31 for the past five years:

	($ millions)				
	1995	**1994**	**1993**	**1992**	**1991**
Non-controlling interest	18.6	17.3	17.4	17.4	17.0
Subordinated convertible debenture					7.5
Shareholders' equity	472.6	391.9	279.5	143.8	116.8
	491.2	409.2	296.9	161.2	141.3

Fairfax's consolidated balance sheet as at December 31, 1995 continues to reflect significant financial strength. Fairfax's shareholders' equity has increased from $391.9 million at December 31, 1994 to $472.6 million at December 31, 1995.

In 1995 the company purchased and cancelled 85,100 subordinate voting shares at an average price of $81 per share.

On October 12, 1994 the company issued 1,000,000 subordinate voting shares at $76 per share, raising net proceeds of $74.4 million. On November 26, 1993 the company issued 2,000,000 subordinate voting shares at $55 per share, raising net proceeds of $104.8 million. Average net outstanding shares increased as a result of these issues from 6,154,254 in 1993 to 8,173,706 in 1994. 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 earnings per share and book value per share figures.

A common measure of capital adequacy in the property and casualty industry is the premiums to surplus (or common shareholders' equity) ratio. This is shown for the insurance subsidiaries of Fairfax for the past five years in the following table:

Net

Premiums Written to Surplus

(Common

Shareholders' Equity)

	1995	1994	1993	1992	1991
Markel 1.6:1	1.3:1	1.1:1	1.0:1	0.4:1	
Federated	1.2:1	0.9:1	1.1:1	1.1:1	1.1:1
Commonwealth	0.7:1	0.8:1	0.7:1	0.6:1	0.4:1
Ranger	1.2:1	1.5:1	1.6:1		
Lombard	2.0:1	2.3:1			
Canadian insurance industry	1.3:1	1.4:1	1.4:1	1.4:1	1.3:1
U.S. insurance industry	1.2:1	1.4:1	1.3:1	1.4:1	1.4:1

In Canada, property and casualty companies are regulated by the Office of the Superintendent of Financial Institutions on the basis of their Section 516 surplus. At December 31, 1995 Fairfax's Canadian property and casualty insurance subsidiaries had a consolidated Section 516 surplus of approximately $275 million (1994 $172 million), significantly in excess of minimum requirements.

In the U.S., the National Association of Insurance Commissioners (NAIC) developed a model law and risk-based capital (RBC) formula designed to help regulators identify property-casualty insurers that may be inadequately capitalized. Under the NAIC's requirements an insurer must maintain total capital and surplus above a calculated threshold or face varying levels of regulatory action. The threshold is based on a formula that attempts to quantify the risk of a company's insurance, investment and other business activities. Fairfax does not anticipate any adverse effects of such requirements because of the strong capitalization of Ranger. At the end of 1995 Ranger had capital and surplus in excess of five times the authorized control level.

Fairfax and its insurance subsidiaries are rated as follows by the respective rating agencies as at December 31, 1995:

	A.M. Best	Standard & Poor's	Duff & Phelps	DBRS	Moody's
Fairfax		BBB+	BBB+	BBB (high)	Baa3
Commonwealth A		A	A+		
Federated	A				
Ranger	A		A		
Lombard	A				
Markel	B++				

In 1995 Fairfax's senior unsecured debt was upgraded to a BBB+ by S&P and Duff & Phelps. Moody's provided Fairfax an initial rating of Baa3. A.M. Best upgraded Federated to an A (excellent), while S&P and Duff & Phelps upgraded Commonwealth to an A and an A+ respectively. Duff & Phelps also provided Ranger with an initial A rating.

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's parent company-only income statement is disclosed on page **XX**. As shown, Fairfax had revenue of $42.5 million in 1995, consisting dividends from its insurance subsidiaries ($27.3 million), management fees ($8.7 million), interest income ($3.9 million) and realized gains from the sale of securities ($2.6 million). After interest expense ($19.4 million), operating expenses ($5.1 million) and non-recurring expenses ($4.1 million), the parent company (or holding company) had income of $13.9 million before taxes. As inter-company dividends are tax free the parent company paid no income taxes, so that net income after taxes amounted to $13.9 million. This income statement shows that in 1995 Fairfax comfortably met all its obligations from internal sources.

In 1996 Fairfax has access to at least the same amount of dividends and management fees and given the elimination of non-recurring expenses, should again comfortably meet all its obligations from internal sources.

For the first time since current management took over the company in September 1985, Fairfax has a large cash holding of $70 million available to meet unexpected requirements. The cash in the holding company would permit Fairfax to meet its interest and other expenses for two to three years without access to any dividends from its insurance subsidiaries.

Also, Fairfax has $215 million of unused, unsecured, committed, five year bank lines. The principal covenant attached to these lines is a covenant to maintain a net debt to equity ratio not exceeding 1:1.

During 1995 Fairfax raised US$100 million in unsecured 8¼% debentures due October 1, 2015 through a public issue in the United States. These funds were used to pay off the long term bank debt of $60 million.

During 1994 Fairfax raised $74.4 million through the share issue referred to above under "Capital Resources". A further $60 million in five year unsecured bank loans provided the balance of the cash component of the purchase price of Lombard. Payment of the purchase price was completed by the issue of an unsecured $25 million 7¾% debenture due December 15, 2003 containing the same terms as the publicly issued debentures.

The debt to equity ratio, net of cash in the holding company, with Lindsey Morden equity accounted was 0.48:1 at December 31, 1995, down from 0.56:1 at December 31, 1994. This improved ratio is still close to the maximum with which Fairfax feels comfortable.

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

Issues and Risks

The following issues and risks, among others, should also be considered in evaluating the outlook of the company.

Claims Reserves

The major risk that all property and casualty insurance companies face is that the provision for claims is an estimate and may be found to be deficient in the future for a variety of reasons including unpredictable jury verdicts, expansion of insurance coverage to include exposures not contemplated at the time of policy issue (e.g. pollution, breast implants), or poor weather. The provision for claims amounted to $913 million on Fairfax's balance sheet as at December 31, 1995.

Reinsurance Recoverables

Most insurance companies reduce their liability for any insurance claim by reinsuring amounts in excess of the maximum they want to retain. This reinsurance does not relieve the company of its primary obligation to the insured. Reinsurance recoverables can become an issue mainly due to solvency concerns but also due to policy disputes. Fairfax had $470 million recoverable from reinsurers as of December 31, 1995.

Catastrophe Exposure

Insurance companies are subject to losses from catastrophes like earthquakes, windstorms or hailstorms, which are unpredictable and can be very significant.

Prices

Prices in the insurance industry are cyclical and can fluctuate quite dramatically. With under-reserving, competitors can price below underlying costs for many years and still survive.

Foreign Exchange

The company has assets, liabilities, revenue and costs that are subject to fluctuations in the U.S. dollar (which have been very significant in the past).

Cost of Revenue

Unlike most businesses, the insurance business can have enormous costs that bear no relation to revenue. Similar to short selling in the stock market (selling shares not owned), there is no limit to the losses that can arise from most insurance policies.

Regulation

Insurance companies are regulated businesses which means that Fairfax does not have access to each insurance company's net income and shareholders' capital without the approval of the insurance regulatory authorities.

Common Stock Holdings

The company has a significant amount of common shares in its portfolio. As common stocks fluctuate, the company's shareholders' equity (or surplus) is exposed to fluctuations in the stock market.

Goodwill

Most of the goodwill on the balance sheet comes from Lindsey Morden. Continued profitability is essential for there to be no deterioration in the carrying value of the goodwill.

Ratings

The company has excellent claims paying and debt ratings by the major rating agencies in North America. As financial stability is very important to its customers, the company is vulnerable to downgrades by the rating agencies.

Holding Company

Being a small company, Fairfax is very dependent on strong operating management, which makes it vulnerable to management turnover.

Quarterly Data (unaudited)

(in $ millions except per share data)

First	**Second**	**Third**	**Fourth**	**Full**	
Years ended December 31	**quarter**	**quarter**	**quarter**	**quarter**	**year**
1995					
Revenue	266.0	281.0	294.8	303.7	1,145.5
Net income	13.4	13.8	18.1	42.2	87.5
Earnings per share	$1.50	$1.53	$2.02	$4.74	$9.79
1994					
Revenue	145.1	153.0	152.2	184.6	634.9
Net income	5.9	8.1	8.4	15.7	38.1
Earnings per share	$0.75	$1.01	$1.05	$1.85	$4.66

Stock Prices

Below are The Toronto Stock Exchange high, low and closing prices of subordinate voting shares of Fairfax for each quarter of 1995 and 1994.

	First quarter	**Second quarter**	**Third quarter**	**Fourth quarter**
	($)	*($)*	*($)*	*($)*
1995				
High	79.00	82.00	86.00	100.00
Low	66.25	72.50	79.00	78.00
Close	73.00	79.00	81.00	98.00
1994				
High	75.00	70.00	76.00	75.00
Low	61.50	59.00	52.00	66.00
Close	67.50	59.00	74.00	67.00

Fairfax Insurance Companies
Combined Balance Sheets
as at December 31, 1995 and 1994

(unaudited)

	1995 *($000)*	**1994** *($000)*
Assets		
Accounts receivable	369,094	334,407
Income taxes refundable	18,911	
Prepaid expenses	7,661	5,392
	395,666	339,799
Cash and short term investments	252,500	261,092
Bonds at book value	799,507	793,113
Preferred stocks at book value	155,646	158,941
Common stocks at book value	388,219	320,739
	1,595,872	1,533,885
Deferred premium acquisition costs	83,859	82,656
Deferred income taxes	38,046	42,875
Capital assets	20,987	18,113
Other assets	21,369	24,286
	2,155,799	2,041,614
Liabilities		
Accounts payable and accrued liabilities	139,009	151,274
Premium deposits	10,929	7,541
Income taxes payable		5,244
	149,938	164,059
Provision for claims	912,655	921,674
Unearned premiums	431,533	417,318
	1,344,188	1,338,992
Shareholders' Equity		
Capital stock	319,031	313,746
Contributed surplus	21,157	12,571
Retained earnings	321,485	212,246
	661,673	538,563
	2,155,799	2,041,614

Fairfax Insurance Companies
Combined Statements of Earnings
for the years ended December 31, 1995 and 1994

(unaudited)

	1995	1994
	($000)	*($000)*
Revenue		
Premiums earned	829,340	400,559
Expenses		
Losses on claims	614,060	296,641
Operating expenses	146,759	82,391
Commissions, net	109,404	38,407
	870,223	417,439
Underwriting loss	(40,883)	(16,880)
Investment and other income (expense)		
Interest and dividends	86,274	53,742
Realized gains on investments	70,302	24,654
	156,576	78,396
Other	(12,773)	(2,510)
	143,803	75,886
Earnings before income taxes	102,920	59,006
Provision for income taxes	2,418	5,350
Net earnings	100,502	53,656

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

Fairfax with Equity Accounting of Lindsey Morden
Consolidated Balance Sheets
as at December 31, 1995 and 1994
(unaudited)

	1995 *($000)*	**1994** *($000)*
Assets		
Cash and short term investments	70,354	7,242
Accounts receivable	369,811	338,261
Income taxes refundable	19,501	8,129
Prepaid expenses	7,781	5,512
	467,447	359,144
Portfolio investments		
Subsidiary cash and short term investments	255,684	262,490
Bonds (market value $821,244; 1994 $775,564)	799,507	793,113
Preferred stocks (market value $160,298; 1994 $157,623)	154,646	158,941
Common stocks (market value $373,990; 1994 $314,484)	386,907	326,568
Total (market value $1,611,216; 1994 $1,509,961)	1,596,744	1,541,112
Investment in Lindsey Morden	28,107	26,036
Deferred premium acquisition costs	84,859	82,656
Deferred income taxes	38,046	42,875
Capital assets	20,987	18,113
Goodwill	14,675	18,297
Other assets	18,112	19,084
	2,268,977	2,107,317
Liabilities		
Accounts payable and accrued liabilities	143,266	143,555
Premium deposits	10,929	7,541
	154,195	151,096
Provision for claims	912,655	921,674
Unearned premiums	431,533	417,318
Long term debt	298,040	225,280
	1,642,228	1,564,272
Shareholders' Equity		
Capital stock	225,295	227,803
Retained earnings	247,259	164,146
	472,554	391,949
	2,268,977	2,107,317

Fairfax with Equity Accounting of Lindsey Morden
Consolidated Statements of Earnings
for the years ended December 31, 1995 and 1994
(unaudited)

	1995 *($000)*	**1994** *($000)*
Revenue		
Premiums earned	829,340	400,559
Interest and dividends	90,144	57,973
Realized gains on investments	71,912	20,026
Equity earnings of Lindsey Morden, net of dividends	2,098	285
	993,494	478,843
Expenses		
Losses on claims	614,059	296,641
Operating expenses	161,013	89,914
Interest expense	19,086	10,426
Commissions, net	109,404	38,407
	903,562	435,388
Earnings before income taxes	89,932	43,455
Provision for income taxes	2,435	5,350
Net earnings	87,497	38,105
Net earnings per share	$9.79	$4.66

Lindsey Morden Group Inc.
Consolidated Balance Sheets
as at December 31, 1995 and 1994

	1995 ($000)	1994 ($000)
Assets		
Cash	996	1,295
Accounts receivable	30,341	25,673
Claims in process	15,390	14,842
Prepaid expenses	1,721	1,604
	48,448	43,414
Capital assets	12,777	11,719
Other assets	35,611	40,775
	96,836	95,908
Liabilities		
Bank indebtedness	7,621	8,875
Accounts payable and accrued liabilities	17,824	16,744
Long term debt current portion	1,672	898
Deferred income taxes	3,883	3,777
	31,000	30,294
Long term debt	11,947	14,626
Future retirement payments	6,614	7,021
	18,561	21,647
Subordinated convertible debenture	8,149	8,519
Shareholders' Equity		
Capital stock	22,618	22,527
Retained earnings	16,508	12,921
	39,126	35,448
	96,836	95,908

Lindsey Morden Group Inc.
Consolidated Statements of Earnings
for the years ended December 31, 1995 and 1994

	1995 ($000)	1994 ($000)
Revenue	154,914	156,093
Cost and expenses		
Cost of service	120,631	116,846
Selling, general and administration	23,325	31,475
Interest	2,875	2,770
Loss on disposal of assets		1,967
	146,831	153,058
Earnings before income taxes	8,083	3,035
Income taxes	4,020	1,997
Net earnings	4,063	1,038

Consolidated Statements of Retained Earnings

for the years ended December 31, 1995 and 1994

	1995 ($000)	1994 ($000)
Retained earnings - beginning of year	12,921	12,364
Net earnings for the year	4,063	1,038
Dividends	(476)	(481)
Retained earnings - end of year	16,508	12,921

These condensed financial statements have been prepared from the Lindsey Morden Group Inc. audited consolidated financial statements as at and for the years ended December 31, 1995 and 1994, copies of which are available on request.

Fairfax Financial Holdings Limited
Unconsolidated Balance Sheets (equity accounted)
as at December 31, 1995 and 1994

(unaudited)

		1995	1994
		($000)	*($000)*
Assets			
Insurance companies			
Ranger		195,268	178,102
Lombard		172,105	158,997
Commonwealth		127,191	113,862
Federated		52,927	51,528
Markel		52,163	42,502
CRC (Bermuda)		40,875	6,453
Wentworth		13,185	9,302
		653,714	560,746
Lindsey Morden	common shares	20,207	18,136
	debentures	7,900	7,900
		28,107	26,036
Hamblin Watsa		10,967	12,367
Real estate		565	1,248
Cash and portfolio investments		75,202	15,991
		768,555	616,388
Other assets		2,217	1,996
		770,772	618,384
Liabilities			
Accounts payable		178	1,155
Long term debt		298,040	225,280
		298,218	226,435
Shareholders' Equity			
Capital stock		225,295	227,803

Retained earnings	247,259	164,146
	472,554	391,949
	770,772	618,384

Fairfax Financial Holdings Limited
Unconsolidated Statements of Earnings
(parent company-only income statement)
for the years ended December 31, 1995 and 1994

(unaudited)

		1995	**1994**
		($000)	*($000)*
Revenue			
Dividend income		27,302	16,685
Interest income		3,898	1,784
Management fees	8,736	4,346	
Realized gains (losses)		2,610	(163)
		42,546	22,652
Expenses			
Interest expense	19,420	11,327	
Operating expenses		5,061	4,529
Non-recurring expenses		4,131	
		28,612	15,856
Net earnings		13,934	6,796

Consolidated Financial Summary *(in $ millions except share and per share data)*

	Return on average share-holders' equity	Per Share Share-holders' equity	Per Share Net earnings fully diluted	Revenue	Earnings before income taxes	Net earnings	Total assets	Invest-ments	Net debt*	Share-holders' equity	Shares outstand-ing at year-end *(000)*	Closing stock price
For the years ended December 31:												
1985		2.08	(1.89)	17.0	(0.9)	(0.9)	41.5	32.7		10.4	5,000	3.25
1986	25.4%	5.89	1.35	53.7	9.1	6.5	129.8	95.6	2.8	41.3	7,007	12.75
1987	31.3%	8.32	2.23	113.0	18.2	16.0	185.4	124.0	2.8	61.0	7,337	12.37
1988	21.2%	10.13	1.94	133.6	21.3	14.4	246.8	137.5	28.2	74.2	7,322	15.00
1989	20.3%	12.41	2.25	125.8	19.2	16.7	248.1	133.9	22.0	90.8	7,316	18.75
1990	23.0%	17.29	2.92	195.4	23.2	21.3	536.0	335.7	65.9	94.7	5,477	11.00
1991	21.3%	21.41	3.94	250.0	32.5	22.5	516.6	341.2	51.3	116.8	5,455	21.25
1992	7.7%	23.76	1.76	286.8	7.0	10.0	590.5	396.2	68.2	143.8	6,055	25.00
1993	20.3%	35.13	5.42	344.0	46.7	33.3	1,200.3	848.8	132.4	279.5	7,955	61.25
1994	12.1%	43.77	4.66	634.9	46.0	38.1	2,173.4	1,551.3	225.3	391.9	8,955	67.00
1995	20.1%	53.28	9.79	1,145.5	95.9	87.5	2,332.9	1,668.1	227.6	472.6	8,869	98.00

* Total debt (beginning in 1995, net of cash in the holding company) with Lindsey Morden equity accounted

** When current management took over in September 1985

Readers of the Management's Discussion and Analysis should review the entire Annual Report for additional commentary and information.

Directors of the Company

Winslow W. Bennett
President, Winwood Holdings Ltd.

† Robbert Hartog
President, Robhar Investments Ltd.

† Steven A. Markel
Vice Chairman
Markel Corporation

Kenneth R. Polley
President and Chief Executive Officer
Lindsey Morden 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.

Kenneth R. Polley
President
Lindsey Morden Group Inc.

Byron G. Messier
President
Lombard General Insurance Company of Canada

Mark J. Ram
President
Markel Insurance Company of Canada

Peter M. Wallner
President
Ranger Insurance Company

Officers of the Company

Brenda Adams
Vice President and 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

Head Office

95 Wellington Street West
Suite 800
Toronto, Ontario M5J 2N7
Telephone (416) 367-4941

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, April 17, 1996 at 4.30 p.m. at the Design Exchange (the old Toronto Stock Exchange building), 234 Bay Street, Toronto.