



Checking in on One of Canada's Super Investors

Description

Something that all investors should do is keep tabs on at least a handful of the world's "super-investors". Thanks in large part to the internet, this really isn't all that hard to do and you never know what brilliant insights you might glean.

Our very own super-investor

Known as the Canadian Warren Buffet, Prem Watsa, Chairman and CEO of **Fairfax Financial** ([TSX:FFH](#)), is perhaps the most publicly accessible Canadian "super-investor" that we have. His [annual letters](#) are a fantastic read and his investment outlook is essentially made available whenever Fairfax reports quarterly results.

Yesterday's release of the company's second quarter results allowed us to check in on how Prem is currently thinking about the world of investing.

He's been bearish on equities for some time and has expressed this view by hedging this portion of the portfolio. According to yesterday's release, nothing has changed. The hedges remain, and as equity markets, especially the one south of the border, keep ticking higher, the more painful these hedges become.

Ouch

Fairfax exited the quarter with equity hedges that amounted to 109% of the company's equity and equity related holdings. This was above the targeted hedge of 100%. Over the first 6 months of 2013, this hedge has resulted in an unrealized loss of \$593 million.

And not only is the company hedged, there is also \$7.5 billion, or 29% of the portfolio, of cash kicking around. This serves as dry powder for the day when more attractive opportunities exist.

During today's conference call, Watsa explained this rather defensive, and expensive stance:

“We continue to be very concerned about the prospects for the financial markets and the economies of North America and Western Europe, accentuated, as we have said before, by potential weakness in China.

As we have said now for some time, there continues to be a big disconnect between the financial markets and the underlying economic fundamentals.”

Why this is so

I once heard Watsa explain the difference between how he manages money and how a portfolio manager of a mutual fund manages money. Mutual fund managers typically care about one thing, relative performance. As long as they beat their benchmark, they don't really care about their returns. They could lose 75% of a portfolio's value in a year, but if the benchmark went down 80%, they win.

Watsa relies on his investment portfolio to make money. He lives in a world of absolute, not relative, performance. If he's right, and the world's financial markets are set for a tumble, and if he's not protected, depending on the severity of this tumble, he could conceivably lose the entire company.

While protecting against this scenario may end up costing him a lot of money if it doesn't play out, he's not going to lose the company because of it.

Investing in the relative world of mutual funds vs. the reality of investing in the world of absolute returns involves completely different strategies and thought processes.

Foolish Takeaway

Because of the hedges that Fairfax has in place, and the cash on hand, it makes the company a very intriguing contrarian bet. If Watsa is right and equity markets begin to unwind, these big unrealized losses will quickly turn into big-time gains. Watsa will have cash at just the time you want a super-investor to have cash and Fairfax shareholders will once again benefit from his superior insight.

Our special **FREE** report “**3 U.S. Stocks That Every Canadian Should Own**” profiles 3 companies that every super-investor would be proud to own. Simply [click here now](#) to download a copy of this report at no charge.

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1. Investing

TICKERS GLOBAL

1. TSX:FFH (Fairfax Financial Holdings Limited)

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Date

2025/08/24

Date Created

2013/08/02

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