



## The Fairfax Financial Holdings Ltd Insider Trading Probe: Should Investors Worry?

### Description

**Fairfax Financial Holdings Ltd** ([TSX: FFH](#)) confirmed on July 31 that Chief Executive Officer Prem Watsa and President Paul Rivett are being investigated by Quebec's securities regulator as part of a probe into possible insider trading and tipping.

Insider trading occurs when an individual or organization uses non-public corporate information to trade stocks. Normally, this happens shortly before important information is made available to the public, thus giving the offender an unfair advantage.

Tipping refers to the act of passing along insider information to another person or organization. The third party then uses the tip to trade the stock of the company involved.

Fairfax Financial disclosed news of the investigation in its Q2 2014 financial results filing.

Prem Watsa, Fairfax Financial's billionaire founder, told analysts on an August 1 conference call that "I can say there is no personal trading involved."

Watsa went on to reassure analysts he and President Paul Rivett are confident that they did nothing wrong.

### Company profile

Fairfax Financial is a financial services holding company with subsidiary operations in property and casualty insurance businesses, as well as reinsurance. However, it also holds significant positions in other industries.

Watsa, Fairfax's billionaire founder, is famous for making contrarian bets.

Fairfax has recently become a top holder of **BlackBerry Ltd.** ([TSX: BB](#))(NASDAQ: BBRY), Canada's beleaguered mobile communications company.

In 2011, he made a bold and profitable investment in the **Bank of Ireland** (NYSE: IRE).

In April, Fairfax announced it was taking a significant position in Greece's third-largest lender, Eurobank Ergasias SA.

Another Fairfax investment was Montreal-based toy maker Mega Brands Inc. which was bought by **Mattel Inc.** ([NASDAQ: MAT](#)) in February of this year. Fairfax owned a 21% stake in Mega Brands before the sale. Once news of the deal was released, Mega Brands' shares jumped nearly 40%.

### **Solid second-quarter earnings**

Fairfax reported solid Q2 2014 net earnings of \$363.7 million compared to a net loss of \$157.8 million for the same period in 2013. Gains in the company's investment portfolio, as well as improved underwriting results, drove profits higher.

Fairfax has a strong balance sheet, finishing the second quarter with cash and marketable securities of \$1.1 billion.

Watsa said the company had excellent underwriting performance in the first half of 2014.

The Fairfax CEO also said, "We are maintaining our defensive equity hedges as we remain concerned about the financial markets and economic outlook."

As of June 30, 2014, equity hedges represented approximately 85% of the company's equity and equity-related holdings.

### **Investor takeaway**

The market doesn't appear to be very concerned about the insider trading investigation, preferring to focus more on the strong earnings report. After the news and the conference call, the stock finished the day at \$518 per share, up \$4.65.

Analysts were also impressed with the Q2 numbers. Equities researchers at BMO Capital Markets hiked their target price for Fairfax from \$500 per share to \$540.

Despite the muted response in the markets, I recommend investors sit on the sidelines any time senior executives are named in a securities investigation.

The canary in the coal mine in this whole ordeal might be Watsa's own view of the financial markets and the global economy. Watsa is respected as a savvy investor and is often regarded as Canada's version of Warren Buffett.

If Watsa says he is concerned about financial markets and the economic outlook, and has put significant hedges in place to protect his equity holdings, it might be best for investors to sit tight and wait to see if the legendary investor is right.

A broad drop in the stock market will bring most companies lower. Investors looking to pick up Fairfax Financial Holdings Ltd might have an opportunity to take advantage of the fall that Watsa is hedging against.

## CATEGORY

1. Investing

## TICKERS GLOBAL

1. NASDAQ:MAT (Mattel, Inc.)
2. NYSE:BB (BlackBerry)
3. TSX:BB (BlackBerry)
4. TSX:FFH (Fairfax Financial Holdings Limited)

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## Date

2025/08/24

## Date Created

2014/08/04

## Author

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