Should Investors Hold Fairfax Financial Holdings Ltd.?

Description

Fairfax Financial Holdings Ltd. (TSX:FFH) released its third-quarter earnings on November 2, and the results were about what I expected them to be. And with a small pullback, investors are curious if they should be picking up shares of this insurance juggernaut.

Let's dive into the quarter to figure that out.

On the whole, Fairfax had net earnings of US$479.6 million, despite this being a historic hurricane season with multiple category five storms hitting regions in the Gulf of Mexico. Hurricanes Harvey, Irma, and Maria cost US$929.5 million (before taxes). In total, this hurricane season was the costliest on record.

Across the different insurance brands that Fairfax owns, it wrote US$2.78 billion in premiums, yet its underwriting loss was US$833 million. However, Fairfax brought in US$1.1 billion in investment net gains, which is what ultimately allowed the company to be profitable, despite these mega-storms costing the company so much money.

And that's an important detail because it's what makes insurance companies worth considering. Under normal circumstances, Fairfax operates with what is known as float, which is the difference between the premiums and the claims made by clients. If Fairfax brings in $1 million in premiums and has to pay out $900,000 in claims, that $100,000 difference is money Fairfax can use to invest. Thanks to that float, Fairfax was profitable, despite the hurricanes.

During the third quarter, Fairfax also sold First Capital to Mitsui Sumitomo Insurance Company, which is based in Tokyo. First Capital is the largest commercial property and casualty insurer in Singapore. In total, Mitsui paid Fairfax US$1.6 billion for the brand, and after tax, Fairfax expects to bring in over US$900 million. Consider that Fairfax only paid US$25 million in 2002, so this is an incredible return — 25% per year.

CEO Prem Watsa summed it up quite nicely in the earning's release: "Fairfax expects to have an excellent year in 2017 in spite of the catastrophe losses, with cash and marketable securities at record levels — and we are prepared if a hard market develops in 2018."

With all of this in mind, should investors pick up shares?

The last time I wrote about Fairfax was at the end of July. At the time, shares were just under $600. With the run-up over the past few months, investors that bought when I recommended are certainly quite happy. However, fellow Fool writer Kay Ng believes that this is a worthy buy if shares pull back to $608. Although the company is in an incredible position, it is possible that the stock could pull back even more from the nearly $700 it was trading at before its results were announced.

Nevertheless, I'm not a market timer, so I wouldn't be opposed to picking up some shares now and then buying on any dips that occur.

However, if you already hold Fairfax, I wouldn't change a thing. Fairfax pays a pretty secure 1.93% yield, so I would just continue pocketing that money as it comes in. And if shares do pull back, you can expect Fairfax to continue its strategy of buying up shares. Fairfax got through hurricane season while still generating a profit, so the next couple of quarters should be quite lucrative.

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