FAIRHOLME CAPITAL MANAGEMENT, L.L.C.

Fairholme Capital Management Public Conference Call

Bruce Berkowitz

Moderator: Daniel Schmerin

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EDITED FOR CLARITY AND ACCURACY

Operator: Good morning. My name is Brandy and I will be your conference operator today. At this time, I'd like to welcome everyone to the Fairholme Capital Management 2016 Public Conference Call.

Bruce Berkowitz, the firm's founder and Chief Investment Officer, will be answering questions submitted in advance by callers. Moderating the call today is Daniel Schmerin, Fairholme's Director of Investment Research.

All lines may be muted to prevent background noise from compromising sound quality. After the call, a transcript will be made available on our site at: www.fairholmefunds.com

Daniel Schmerin: Good morning, I'm Daniel Schmerin, Director of Investment Research at Fairholme Capital Management. I'd like to welcome Fairholme shareholders and other listeners to our 2016 Conference Call.

I'd like to begin by expressing our appreciation to all of those who took the time to submit thoughtful questions for our call today. Without further ado, I'd like to introduce Bruce Berkowitz, our Founder and Chief Investment Officer.

Bruce Berkowitz: Thanks Dan, and good morning to everyone. It's a pleasure to be hosting this call today. Before we dive into your questions, I would like to make a few opening remarks.

First, for those of you who have invested with us for many years, and those who have invested with us more recently, I thank you for the trust and confidence you've placed in our hands. Fairholme is a family, we are not a large firm. Through thick and thin, we remain intensely focused on one overriding objective: and that is to generate above-average total returns for our investors over time.

As you know, we take unconventional approaches to investing. Our clients expect us to beat to a different drum. They expect us to ignore the crowd, and they expect us to focus on our best opportunities, as we said we would since inception of the fund. We continue to do this day in and day out.

We continue to follow a time-tested approach that has worked for Fairholme. We are contrarian, not for the sake of being contrarian, but contrarian as a result of our research work to find bargains. Three decades of experience have taught me that this is the safest investment approach and the safest way to meet our investment objectives. Avoiding permanent loss of capital is the number one rule. That's how wealth is created over time.

I know that recent times have not been easy for any of us shareholders. And at Fairholme, we experience many of the same emotions as our investors. After all, Fairholme is personal and I have always had my family's entire liquid net worth fully invested in Fairholme products.

We set a very high bar for ourselves at Fairholme, particularly with respect to performance. I expect us to surpass that bar. When we fall short, as we did in 2014 and 2015, I can assure you that we assess whether our analysis is flawed or whether the market temporarily disagrees with our perspective.

If our analysis remains sound, but few other market participants agree, we rely upon conviction, courage, and fortitude – and we tend to buy more at cheaper prices. Running with the crowd is easy, but that's not what we do. Separating from and ultimately leading the pack is harder.

Dan, given my years in this business, I'd like to provide some context to today's environment. It's very reminiscent of my experience in the late 80s and early 90s. At that time, Wells Fargo was constantly testing new lows, plunging on fears of its California real estate loan exposure. The market was unbelievably fearful, and the company's share price was trading at just two times pre-tax, pre-provision earnings. I strongly disagreed with the market, but that didn't mean it was easy or pain-free. I calculated that Wells Fargo was worth many multiples of its distressed trading price back then. And with conviction and courage, I built up the position until it was by far my largest holding, and boy did I look wrong. In fact, I continued to look wrong for several years after I initiated the investment. However, by the late 90s, Wells Fargo's share price dramatically increased – it was a seven bagger.

Today, when I compare our current positions to that investment journey, or if I think about more recent successes like General Growth Properties and AIG, I can't help but conclude that our current portfolio has as much, if not more performance potential than any of the past investments. I want to make sure we address the key points for our core positions today, and that we answer the most popular questions submitted.

Daniel Schmerin: That provides a good segue into our first question: in the Fairholme Fund's Annual Letter published last month, you indicated that "times have changed" and that "if markets remain less liquid, we will become less concentrated than in the past." Does that mean Fairholme will become a diversified fund?

Bruce Berkowitz: Rest assured, it is not in Fairholme's DNA to manage index-like, broadly diversified funds. When I started the Fairholme Fund just over 16 years ago, our investment philosophy was straightforward: focus on best ideas; buy at a cheap price; it's all about what you pay versus what you receive. What you give versus what you get, price versus value, with a focus on best ideas. That remains true today, and all of our core positions fit that profile.

Again, we can look quite wrong until we are perceived to be right. That's the hard part. We do look very wrong today based on market prices. As you know, there is no free lunch. Mr. Market will make you work for it. But eventually, I believe, when investor emotions change or deeply buried facts emerge, the price pendulum swings back to a more normal positioning. In the commentary in my Annual Letter to shareholders, I tried to shed some light on why we adjusted positions, and how position sizing is affected by a host of factors.

Consider this: in the past 16 years of the Fairholme Fund's life, there have been only three periods when the Fund's performance has landed it in the bottom quartile. 2003 was followed by four years of absolute and relative outperformance. 2011 was also followed by two years of absolute and relative outperformance. Our recent performance has put us back in the doghouse, and this is the third such period over the life of the Fund. Some believe that this time is fundamentally different, that the past won't serve as a useful guide, or that the price pendulum may never swing back our way. I'm not going to offer any specific predictions, because everyone knows my timing is not perfect, but I can say this to you: history may not exactly repeat itself, but it does tend to rhyme.

Daniel Schmerin: We received several questions about the long-term capital gains distribution to Fairholme Fund shareholders in late 2015, and how that impacted the Fund's share price.

Bruce Berkowitz: The 2015 distribution represented a very big win on AIG. The distribution of about $13 per share reduced our fund share price by $13 per share. There were two results. For those who take their dividends in cash, it was a bonanza, Christmas came early. For those who reinvest, they earned 30% more shares in the fund the next day. And I am not blind to taxes. I paid my share of those capital gains distributions. In the end, it was just not worth the opportunity cost of attempting to offset gains with losses. I thought our positions were so unique and have so much potential, that to try and sell those with losses, and then regain those positions after a 31 day period would be near impossible.

Daniel Schmerin: On the topic of AIG, people were interested to know why you reduced the Fund's exposure during 2015. Did your view fundamentally change? Isn't it still cheap?

Bruce Berkowitz: As we have written in all of our letters, we bought AIG at substantial discount to tangible book value ("TBV"). We had a simple thesis that AIG still had a franchise value, and that AIG was worth at least TBV. We then started selling in 2014 as our thesis played out and AIG approached our estimate of TBV. That was always our game plan.

We have made a considerable amount of money in AIG, and AIG remains the largest position in the Fairholme Fund in the form of long-dated, double-ratchet warrants, which we received during the recapitalization of AIG in 2011. It is my belief that these double-ratchet warrants have unique features regarding conversion price and conversion ratio, and they can potentially disproportionately benefit from future corporate actions of AIG including asset sales, capital distributions, and dividend payments.

Daniel Schmerin: It is clear you like the AIG warrants over AIG's common stock. What is your view on recent activist efforts?

Bruce Berkowitz: I've followed AIG for decades. The company's configuration is unique. But I believe that underappreciated assets should be sold. I believe that corporate expenses need to be dramatically reduced. Less regulatory restrictions across the entire company would be quite beneficial. AIG can take a lot of actions, and we support all efforts to maximize shareholder value.

Daniel Schmerin: During 2015, you reduced Bank of America common stock across portfolios. What changed? Do you fear another crisis brewing like 2008?

Bruce Berkowitz: Nothing has changed. Again, similar to AIG, in fact same story as AIG. We sold based on TBV. If anything has changed, today the financials are more akin to regulated utilities. All "too big to fail" institutions, except for Fannie Mae and Freddie Mac, have fortress-like balance sheets. And it's harder now for banks to effectively generate a decent return on that fortress-like capital.

Daniel Schmerin: How would you assess Brian Moynihan's leadership to date?

Bruce Berkowitz: Brian has done well with the hand he was dealt. It's not easy to steer such a large organization, but he has been paddling fast. Personally, I think he should spin off Merrill Lynch and U.S. Trust. Those gems are certainly not utilities.

Daniel Schmerin: Let's turn to Leucadia. You've owned it for a long time. What are your thoughts?

Bruce Berkowitz: I have tremendous respect for Mr. Steinberg and Mr. Cumming, who created the company. But it's a different company today. It's a different environment. And there are many industries in stress today. Facts change, we change. We still think highly of the people at Leucadia, but in our rank ordering process, we have found other opportunities to take advantage of.

Daniel Schmerin: Let's move on to the St. Joe Company. Some market participants have interpreted the recent registration statement filed by St. Joe to mean that your view on the company has soured. What's the truth?

Bruce Berkowitz: My view on St. Joe has not soured. The company's regulatory filing was routine. It happened previously in April 2013. It has no bearing on our investment outlook.

The company last year received entitlements spanning 110,000 acres of nearly contiguous land on Florida's Emerald Coast. The company now has the ability to develop 22 million square feet of retail, commercial, and industrial facilities, along with 170,000 residential units. There is huge potential at St Joe.

Daniel Schmerin: So let's drill down on that a little bit and discuss your perspective regarding St. Joe. Particularly, what has been accomplished since you've been actively involved?

Bruce Berkowitz: Dan, I started with four objectives. Stop the bleeding – that is, eliminate excessive corporate spending and other fixed expenses at St Joe. Strengthen the balance sheet is number two, to create huge liquidity to be able to weather any environment. The third objective was to focus the company on core projects that can really move the performance needle. Fourth is helping the company create the underlying conditions for maximum optionality and long-term success. I believe these objectives have been accomplished.

Over the last few years, St. Joe has sold some of its non-core assets. More recently, the company appointed a new CEO, Jorge Gonzalez.

The company is now focusing on creating partnerships with the best, most experienced companies that can help increase the value of St. Joe's land – whether it's the entitlements, the deepwater port, the short-line railroad, the new international airport, the hotel, or the golf and resort properties, there's a whole lot at St. Joe. And I have to tell our shareholders, for those who think St. Joe is just forestry land far away from civilization, you need to come down and visit St. Joe and take a look for yourself.

Daniel Schmerin: Do you need to remain Chairman of the Board for the company to succeed going forward?

Bruce Berkowitz: The short answer is no. The company is now entering a new phase, transitioning from what I consider defense to offense. While I am happy to continue serving, there may well be others who can bring different expertise that will be accretive for St. Joe's next chapter.

Daniel Schmerin: Let's turn to Fannie Mae and Freddie Mac. Shareholders expressed a lot of support for our ongoing efforts. I know that you recently corresponded with a soldier bravely serving overseas in the 5th Marine Expeditionary Brigade.

Bruce Berkowitz: Yes, I was thrilled to receive his message and we should all be grateful for his service. A true patriot. Yet, he is one of thousands upon thousands of our shareholders affected by Fannie Mae and Freddie Mac.

Daniel Schmerin: Give listeners a brief overview of the state of play with respect to Fannie and Freddie.

Bruce Berkowitz: This should be a replay of our experience with AIG. Fannie and Freddie should be treated the same as AIG, and ultimately released of government control.

Let us back up a bit. Fannie Mae and Freddie Mac are absolutely essential to America's housing market. Who else makes the 30-year pre-payable fixed-rate mortgage widely available through thick and thin? Who else can provide $7 trillion of liquidity to America's housing market since 2009 helping low and moderate-income Americans buy, rent, or refinance a home?

Fannie and Freddie are two companies that help all Americans, whether they know it or not. Fannie and Freddie are definitely two of the most valuable companies in the world. It is still hard to believe that some in Washington want to eliminate them in the hope of finding something better, or at least finding something that caters better to their special interests and crony capitalists.

But the Companies are not going away. Fannie Mae is relocating to a new million square foot office complex in downtown Washington, and Freddie Mac just announced that they hired several hundred new employees. If this Presidential Election is any indication, the days of such bureaucratic malfeasance are numbered.

I believe the United States Treasury is growing increasingly isolated as a result of its 8-year policy forcing Fannie and Freddie to remain in a state of captivity known as "conservatorship." It is a shame and a huge delay of game. I am shocked that Senator Corker allowed the President to take $250 billion dollars without Congressional approval, a stunning figure that continues to grow and an action that may well cause the next financial crisis.

Daniel Schmerin: Can you explain the nature of our investments in Fannie and Freddie?

Bruce Berkowitz: We own preferred stock of two of the most successful companies in American history. Preferred stock is not common stock. Preferred stock is a contract, a contract that protects our bundle of economic rights. One of the rights it protects is a liquidation preference, a priority claim with regard to the repayment of principal. The contract is between a buyer and seller, and it is backed by the nation's laws.

The Treasury also owns preferred stock. We own Preferred stock, the Treasury owns preferred stock, and a preferred stock is a preferred stock. But the Department of the Treasury seems to make up the rules as they go. They take everything with their preferred stock, and we don't even receive a return of principal with our preferred stock.

I don't understand why some believe they are above the law, and that they are able to choose who wins and loses. Fairholme and other shareholders aren't seeking anything more than for Treasury to respect the capital structure of each company, to respect the economic bundle of rights associated with our securities and to respect the law setting forth the rules of a conservatorship as decreed by Congress in the passing of the Housing and Economic Recovery Act of 2008 ("HERA").

Daniel Schmerin: A few years have elapsed since you initiated this investment. Do you have more or less conviction in Fannie and Freddie today than when you first bought?

Bruce Berkowitz: We have made enormous progress over the last 12 months, largely behind the scenes. With each passing day, we seem to be getting closer to the finish line, so I remain very optimistic.

We have the facts on our side. Fannie and Freddie are hugely profitable. We have the law on our side. We have common sense on our side, and we have history on our side. Alexander Hamilton, one of our founding fathers, made a momentous decision after the Revolutionary War to recognize the debt of states as federal debt. Hamilton chose not to differentiate between original holders of bonds and those who later bought the bonds from original holders. Hamilton believed it was imperative for our nation to honor all its obligations. So, while a statue of Hamilton sits outside the Treasury Department today, it doesn't seem as though those inside today appreciate that precedent he set, but this will change.

Daniel Schmerin: Perhaps you can you elaborate on some of the progress. There are 22 cases pending across the country challenging the so-called "Net Worth Sweep," the federal government's blatantly illegal expropriation of private shareholders' interests in these two companies, and it seems like there are more complaints filed with each passing month.

Bruce Berkowitz: Dan, anyone who is willing to spend an hour of time understanding the facts ends up shocked and outraged by the government's unlawful actions. There are cases advancing in the District of Columbia, Iowa, Kentucky, Delaware, and Illinois. I expect that there will be judicial decisions on several of these cases this year.

Our lawyers have taken discovery on various topics relating to the Net Worth Sweep in the Court of Federal Claims. Plaintiffs in other courts have now obtained access to these discovery materials and are amending their complaints to make use of this information. Meanwhile, the government is fighting tooth and nail to withhold over 12,000 documents, and I believe those documents contain very incriminating evidence against the defendants.

So, we are advancing the ball down the field strategically and at an increasingly accelerated pace. It doesn't look that way when you take a look at the price of our preferred stock, yet we are making substantial progress.

Daniel Schmerin: To pick up on that, in a speech just last week, Mel Watt, the conservator of Fannie and Freddie, expressed serious concern about the inability of these two companies to retain capital. In fact, he highlighted the escalating risks of this perpetual conservatorship.

Do you believe that Fannie and Freddie will need another bailout?

Bruce Berkowitz: Mel Watt is telling the truth. If you ask Director Watt if the Treasury Department is helping or hurting Fannie and Freddie, do you know what he will say? Treasury is hurting, and in fact making the situation much worse. The Treasury is significantly constraining his ability to effectively manage the conservatorship. He'd tell you that the sheep dog has turned into the wolf.

Fannie and Freddie have over $5 *trillion* of liabilities outstanding, yet Treasury is milking them of all their income and forcing them to operate with no capital. It's absurd. If the government takes all of your wealth every quarter as the return on a forced investment, and never allows the repayment of that forced investment, then it is inevitable that there will come a time in the future when the government will force more investment on you, another so-called bailout.

Through the imposition of the Net Worth Sweep, Treasury usurps all past, present, and future earnings of Fannie and Freddie as so-called "dividends" in order to make repayment impossible. It is illegal. It defies contract, corporate, and investment laws that allow confidence in American financial markets.

But I can understand Treasury's viewpoint. The Net Worth Sweep tries to cement a de facto nationalization of Fannie and Freddie. It has allowed and continues to allow an administration to magically reduce budget deficits and avoid congressional debt ceiling negotiations before presidential elections. I get it. But it is wrong, and it's shortsighted.

Why are all financial institutions except for Fannie and Freddie subject to more stringent capital requirements imposed under Dodd-Frank? Leaving out the two largest financial institutions in the country makes Dodd-Frank toothless. How can you have a designation process for Systemically Important Financial Institutions and not start with Fannie and Freddie? It makes the entire SIFI designation process look like a sham.

Representatives in Congress are just now beginning to learn the truth and consequences of Treasury's actions. Luckily, Director Watt has ample authority to fix this situation. A few days ago in the Financial Times, Fannie Mae CEO Tim Mayopoulos noted that Mel Watt had a range of options for solving the capital problem, such as allowing the companies to retain earnings, changing the terms of Treasury's agreements with each company, and pushing the companies out of conservatorship so they can be recapitalized in another way.

Letting the companies retain what they make would be an awfully useful start to this process – after all Fannie and Freddie made over $17 billion in 2015, and they have repaid the government $250 billion to date.

Daniel Schmerin: That's a lot of money, even in Washington.

Some shareholders have asked whether you believe this investment has a binary outcome, and whether our success hinges solely on a court decision. They also wondered whether there was an alternative dispute resolution mechanism beyond the courts.

Bruce Berkowitz: I don't believe this is a binary outcome. This isn't a light switch, there isn't an on or off, zero or one. That would clearly violate our investment rules. We have a margin of safety: there is no alternative to Fannie and Freddie. They are tremendously profitable. They are not shrinking; they are growing. Sooner rather than later, they will be transformed into low-risk, public utilities with regulated rates of return just like your local water or electric company.

The government can't have its cake and eat it too. It cannot de facto nationalize the two largest financial institutions in America, and pretend that it doesn't have to consolidate their assets and liabilities on the federal balance sheet. Congress did not authorize the Treasury Department to nationalize these two companies. This charade must end soon because our housing market, which comprises 23% of GDP, and our national economy are increasingly at risk. America cannot afford to get this wrong. We remain ready, willing, and able to help explore any feasible option in order to reach a mutually beneficial outcome for all stakeholders. Litigation was not our preferred course of action, but it has proven necessary. Make no mistake, we have been willing to negotiate and compromise from day one. We have been willing to talk constructively with Treasury from the get go.

In 2013, Treasury seemed to believe that Fannie and Freddie were worthless, so a consortium of investors, including Fairholme, offered to buy the insurance businesses of Fannie and Freddie. We received no written response to our offer. More recently, in late 2015, there was settlement communication between plaintiffs and the government, but frankly, given how deep Treasury has dug in its heels and tried to hide the truth by withholding evidence, it remains unclear to me whether Treasury is capable of having an earnest conversation. And the fact that Treasury has sent some staffers to work next door at the White House really raises the specter that the President and his most senior advisors are being purposefully misled.

Daniel Schmerin: Let's move on, we received the most questions about Sears.

How do you evaluate your investment in Sears today?

Bruce Berkowitz: Our thesis on Sears cannot be disproven: Sears has a vast real estate empire complemented by unique businesses. Sears also has constraints, and we understand those constraints. As part of our investment process, we developed progress checklists concerning Sears' fixed obligations, balance sheet strength, footprint, pension fund obligations, the repurposing of real estate, and spinning off companies that would benefit from independence. We thought about all of the possibilities and the potential.

We do understand today that the retail world is morphing, and we understand the challenge of optimizing a huge set of company assets subject to those constraints. On our checklist the two remaining issues are pension fund obligations and retailing losses.

The first, the pension fund obligation, should improve over time, especially with higher interest rates. The other remaining issue, the retail losses, is, in our opinion, voluntary, and is expected to stop this year.

Daniel Schmerin: We received several questions about the mistakes that Sears has made over the years, and the impact that those mistakes have had on our investment.

What are you views?

Bruce Berkowitz: Dan, nobody is perfect, and in hindsight it's easy. Yes, Sears bought back stock too high. Yes, I was way, way too early in buying Sears stock for our shareholders. Yes, Sears' pension obligation has been a larger consumer of cash than I anticipated, due in part to the prolonged low interest rate environment. I did not predict that the pension fund would chew up $2 billion of cash in recent years, which as of today is more than the entire market cap of the company.

Yes, these have been unforced errors that have caused a delay of game. It is taking longer than I thought to maximize and monetize the enormous asset base under the Sears umbrella than we would have expected, but it is happening. Last year's spin-off of 266 properties to a newly formed real estate investment trust called Seritage is proof positive. And the nearly $32 of distributions that shareholders have received from other Sears corporate actions serves as additional proof.

Daniel Schmerin: Is it fathomable that the market is missing the huge gap between Sears' current stock price and our estimate of intrinsic value, which you published in our Annual Letter last month?

Bruce Berkowitz: It's not just fathomable, it's today's reality. Our shareholders have to remember Fairholme's success to date is precisely based on this concept that having a unique viewpoint allows us to buy companies at tremendous discounts. It wasn't that long ago that AIG was perceived to be dead; Bank of America was perceived to be dead; the entire financial system was about to go over the cliff. We disagreed, and we invested in financial companies and helped stabilize those companies to the benefit of our shareholders, and the country recovered.

We expect the same to be true of all our current investments, including Sears. The facts tell us that we own valuable assets at historic discounts. The facts determine our confidence and willingness to stay the course. Either Sears' price is going to climb to our assessment of intrinsic value, or we are wrong about that value and it will decline toward the current stock price. Most likely the stock price and our estimate of intrinsic value will meet somewhere in the middle of this large range of possibilities, the same way it has happened for almost every investment at Fairholme.

Daniel Schmerin: We recognize Sears has spent a considerable amount of money trying to stay competitive in a rapidly changing retail environment.

Has it been worthwhile?

Bruce Berkowitz: I don't know yet. If Sears is able to return to profitability this year, which is the company's most important focus during 2016, then yes it has been worthwhile. A considerable portion of the past cash burn is voluntary based on the transformation of the retail businesses. The remaining portion is based upon the pension and rent expenses, which will go down with time. Again, Sears has been going through this metamorphosis, and its technology spending and Shop Your Way marketing spending has been very costly. However, we expect much of the heavy lifting is over, and those expenses should decline.

Daniel Schmerin: Three shareholders asked about the recent Schedule 13D filing, and the perception that you will push for change at Sears.

So what's the truth?

Bruce Berkowitz: Fairholme owns over 25% of Sears' stock as well as various other Sears-related securities. In mid-December we filed a Schedule 13D on our Sears position. We filed on behalf of our shareholders, and it is important that I express my views to the company. In fact, I was invited to express my views to the company just last month in front of their Board of Directors. I took that opportunity to explain Fairholme's investment perspective on the company as a whole, as well as its various business units.

This included our view regarding the need to preserve the enormous value of its assets and the imperative to promptly return to profitability. I focused on the cash burn, and how the continuation of the cash burn does not build confidence or trust among all of Sears' constituents – I'm talking about Sears' customers, vendors, suppliers, employees, creditors, and investors.

I also discussed my belief that eliminating the cash burn will do more to optimize the value of Sears' assets than any other action. I also shared my view for Sears to help shareholders better understand the company's assets and strategies by giving them more information. The bottom line is not everyone has the ability to spend as much time studying Sears as we do. Most people only focus on stock price, and while it is wrong, it is human nature. I recognize that much of what Sears' management has written has proven true. I recognize that most do not understand the vast asset base at Sears, and I recognize that most do not understand the complexity of optimizing all of the assets. More information and a little more hand holding may be helpful – it sure won't hurt.

I must tell you after I gave my thoughts to the Board and left, I did not sense any disagreement among the Board with any of the points that I raised. I left feeling that we were squarely on the same page. I clearly believe that they know what to do and my views were not revolutionary at all. Also, it is important to note that as I left, there appeared to be an appropriate sense of urgency for these matters.

Daniel Schmerin: Let me then get to one final shareholder question regarding a recent addition to the Fairholme Fund with the ticker DNOW: Distribution Now, a global distributor to the energy and industrial markets.

Can you discuss your investment thesis on this energy company, and oil and gas markets more broadly?

Bruce Berkowitz: Let's rewind the clock a bunch of years. We first invested in energy companies many years ago, in an era when no one thought the world would function with oil prices above $40 per barrel. We sold many of our investments after the price of oil exceeded $100 per barrel. Well, here we are again today, and no one believes that oil prices will rebound. In the immortal words of Yogi Berra, it's déjà vu all over again.

Supply naturally depletes. Oil and natural gas reserves naturally deplete. Meanwhile, demand for oil and gas will not dissipate; in fact, it increases, especially with the conversion we are seeing to natural gas for utilities. Today, we have a situation where the selling price of these commodities is lower than the price to produce them. This can't last – something has to give. Demand will go up, and price must rise to entice producers to supply more. When? We don't know.

So to answer your question on DNOW, we acquired shares in that company as well as its competitor MRC Global. These two companies comprise 5% of the Fairholme Fund's assets, and they are two of the largest players in North America in the energy supplies and distribution segment. They are not making much money in the current environment, but we paid cheap multiples of assets on their balance sheet. The segment is completely fragmented, providing quite an advantage to these companies given their size and scale, and they both are well run.

They lead an industry that is ripe for consolidation. Any uptick in oilfield activity causes the phones to start ringing at these two companies. The parts and supplies they provide are essential to the industry. I believe these two companies should ultimately come together to maximize value for all their shareholders, and we have communicated our views to each company that they should merge.

Daniel Schmerin: Any other parting thoughts for our listeners?

Bruce Berkowitz: Without trying to sound excessively optimistic, I do want our shareholders to know that I am excited about the future for our investments. We are poised for success, and any one win in the investments in our funds can have an unusually outsized impact on performance. I know you share that sentiment, Dan, but saying it aloud doesn't make it easier for our fellow shareholders.

When I mentioned earlier that Fairholme is personal, I meant it. Yes, we eat our own cooking, and that's a good thing. But let me admit, I wasn't pleased when my mother fired me again this year – she wouldn't even talk to me. Quite feisty. Perhaps that's a good omen, because every time she has fired me, we have significantly outperformed thereafter.

I hope she is listening; she should know better than to sell low and buy high. Just makes no sense. But from my perspective, one clear takeaway is that our shareholders, including my mother, are increasingly sensitive to volatility. We need to be responsive to that and the fears that it creates for our own shareholders. After all, what's the point of doing what we do if Fairholme employees are the only ones remaining at the end of the day?

I certainly won't derive any satisfaction if we are the only ones left standing with a big win. Fairholme is family. I intend for us to all succeed together. And I don't intend to allow the last 30 years of hard work go for naught.

Daniel Schmerin: We've covered a lot of material today. Thank you all for taking the time to join us. If you have further comments on what you've heard, please send us a note.

Bruce Berkowitz: And Dan, to our shareholders, if we have not answered your question, feel free to drop by our headquarters in Miami and kick the tires. Please just call ahead.

Thank you, everyone. Onward and upward. Have a nice day.

Operator: Thank you again for participating. This concludes Fairholme's public conference call.

Past performance is not a guarantee of future results.

The opinions of Mr. Berkowitz expressed herein should not be considered a guarantee of future events or future results, or investment advice. Any references to past performance should not be construed as an indicator of future performance. Any projections, market outlooks or estimates that may be included in this material are forward looking statements and based upon certain assumptions. Other events that were not taken into account may occur, and may significantly affect the returns or performance of the Funds. Any assumptions should not be construed to be indicative of the actual events which will occur.

Each Fund's investment objective, risks, charges and expenses must be considered carefully before investing. The prospectus contains this and other important information about investing in the Funds, and it may be obtained by calling (866) 202-2263, or visiting www.fairholmefunds.com. Please read it carefully before investing.

Mutual fund investing involves risk. Principal loss is possible. The Fairholme Fund is non-diversified, which means that The Fairholme Fund invests in a smaller number of securities when compared to more diversified funds. Therefore, The Fairholme Fund is exposed to greater individual stock volatility than a diversified fund. The Fairholme Fund also invests in foreign securities which involve greater volatility and political, economic and currency risks and differences in accounting methods. The Fairholme Fund may also invest in "special situations" to achieve its objectives. These strategies may involve greater risks than other fund strategies.

Portfolio holdings are subject to risk and may change at any time. Any questions you have regarding the latest month-end performance can be obtained by calling shareholder services at (866) 202-2263.

Fairholme Distributors, LLC (2/16)

THE FAIRHOLME FUND

Managed by ***Bruce Berkowitz***

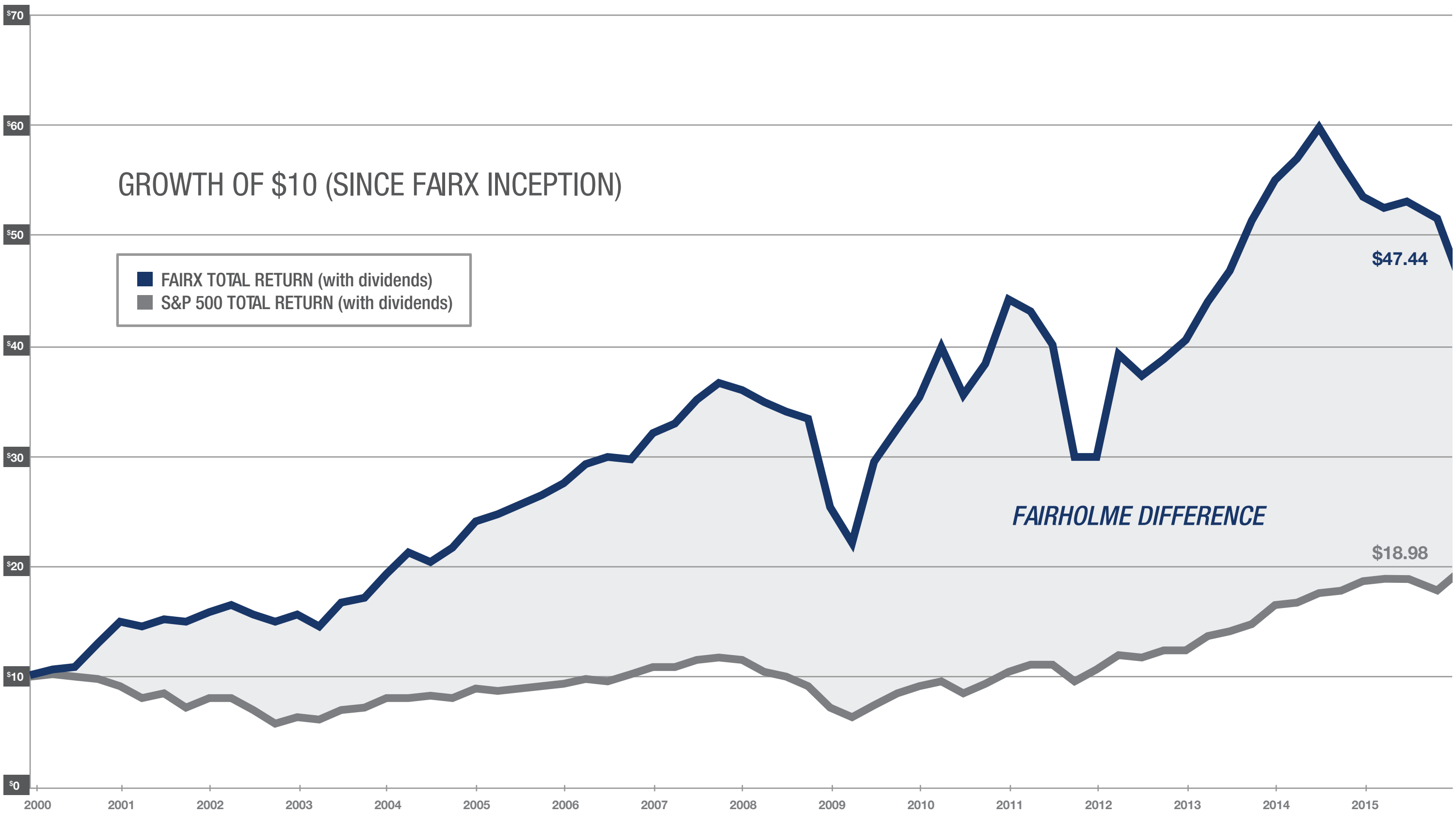
at 12/31/15

Long-term capital growth through a focused portfolio of equity and equity-like securities acquired at prices well below underlying intrinsic values.

Growth of $10 (Since Inception)[1]	
Net Asset Value	$18.50
Distribution Value	$26.13
Reinvestment Value[2]	$2.81
Total Value	**$47.44**

60-Month Rolling Returns	FAIRX	S&P 500
Best	+185.26% (3/2009-2/2014)	+181.57% (3/2009-2/2014)
Average	+69.02%	+37.87%
Worst	-6.89% (1/2007-12/2011)	-29.05% (3/2004-2/2009)
Percentage of Positive Periods[3]	97%	80%

Fund Manager of the Decade[4]
Domestic Equity



The chart above covers the period from inception of the Fund (December 29, 1999) to December 31, 2015. ***Performance information quoted above represents past performance and does not guarantee future results. The investment return and principal value of an investment in the Fund will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. Current performance may be lower or higher than the performance information quoted above. Performance figures assume reinvestment of dividends and capital gains, but do not reflect a 2.00% redemption fee on shares redeemed within 60 days of purchase. Most recent month-end performance and answers to any questions you may have can be obtained by calling Shareholder Services at 1.866.202.2263.*** *The S&P 500 Index is a broad based measurement of changes in the stock market, is used for comparative purposes only, and is not meant to be indicative of the Fund's performance, asset composition or volatility. Given the wide scope of securities held by S&P 500, it should be inherently less volatile. Our results may differ markedly from those of the S&P 500 in either up or down market trends. The performance of the S&P 500 is shown with all dividends reinvested into the index and does not reflect any reduction in performance for the effects of transaction costs or management fees. Investors cannot invest directly in an index. The expense ratio of the Fairholme Fund is 1.06%. The expense ratio includes acquired fund fees and expenses which are incurred indirectly by the Fairholme Fund as a result of investments in securities issued by one or more investment companies.*

Cumulative Return	FAIRX	S&P 500
1-Year	-11.48%	+1.38%
3-Year	+16.71%	+52.59%
5-Year	+7.12%	+80.75%
10-Year	+72.25%	+102.42%
15-Year	+217.09%	+107.99%
Since Inception	+374.42%	+89.81%

Annualized Return	FAIRX	S&P 500
1-Year	-11.48%	+1.38%
3-Year	+5.29%	+15.13%
5-Year	+1.39%	+12.57%
10-Year	+5.59%	+7.31%
15-Year	+8.00%	+5.00%
Since Inception	+10.21%	+4.08%

THE FAIRHOLME FUND

Managed by ***Bruce Berkowitz***

at 12/31/15

Assets	$ Millions
Net Assets	$3,351
Cash and Equivalents[5]	$715
Distributions Paid Since Inception	$4,633
Employee Ownership	$106

Time to Cash[5]	% FAIRX
2-Days	25%
30-Days	50%
178-Days	75%

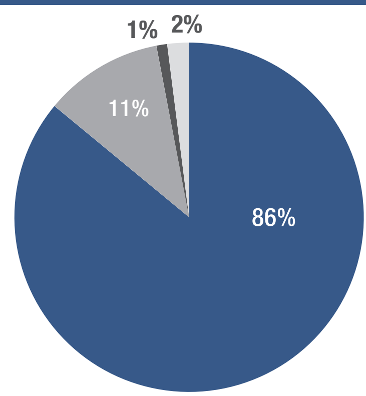
Top Holdings[6]	% FAIRX
Cash and Equivalents[7]	21.3%
AIG	14.2%
Sears Holdings	13.2%
St. Joe	12.8%
Fannie Mae	8.7%
Freddie Mac	7.7%
Imperial Metals Corp	5.4%

Our Philosophy

Focus	Best ideas.
Strategy	Multi-cap value.
Return	Expect better than the S&P 500 Index.
Risk	Market prices may be volatile.
Horizon	5+ Years.

Distribution (Since Inception)

- Long-term Capital Gains
- Income
- Return of Capital
- Short-term Capital Gains



(1) This chart assumes that distributions have been reinvested and does not include the effect of taxes.

(2) This figure represents the appreciation of the reinvested distributions since inception.

(3) This figure represents the percentage of 60-month rolling periods with returns greater than 0% since the inception of The Fairholme Fund.

(4) The Fund Manager of the Decade award (2000-2009) recognizes fund managers who have achieved superior risk adjusted results over the past 10 years and have an established record of serving shareholders well. Morningstar takes into consideration the fund's performance over the past ten years, including the fund manager's strategy, approach to risk, size of the fund, and stewardship. Award winners are selected based on Morningstar's proprietary research and in-depth evaluation.

(5) The time to cash is calculated by determining the amount of days it would take to raise a given percentage of cash in the Fund based on selling 25% of average daily volume for the preceding three-month period.

(6) Percentages of FAIRX were calculated aggregating all securities held of a particular issuer.

(7) Cash and Equivalents include investable cash, money market funds, and commercial paper.

Investing in the Fairholme Fund involves risk including loss of principal. The Fund is non-diversified, meaning it invests in a small number of securities and therefore is exposed to greater individual issuer volatility than a diversified fund. The Fund may focus on issuers undergoing reorganization or other special situations, which may entail greater risk. Any debt securities held by the Fund are subject to credit risk, and some of them may be rated below investment grade, meaning they have greater credit risk. Debt securities usually fall in value when interest rates rise. The Fund may hold foreign securities, which are subject to potential loss from currency fluctuations, limited liquidity, lax regulation, and social instability. Investments in small- and medium-sized companies by the Fund could be more volatile than securities issued by large companies because smaller companies have limited markets and financial resources. The composition of the Fund's portfolio holdings and sector weighting are subject to change and should not be considered recommendations to buy or sell any securities. **Current and future portfolio holdings are subject to risk.**

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The Fund's investment objectives, risks, charges, and expenses should be considered carefully before investing. The prospectus contains this and other important information about the Fairholme Fund, and it may be obtained by calling Shareholder Services at 1.866.202.2263 or visiting our website www.fairholmefunds.com. Read it carefully before investing.