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 would like to welcome everyone to the Fairholme Capital Management ("Fairholme" or the "Firm") November 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. Also joining them on the call is David Thompson, managing partner at Cooper & Kirk and one of the lead attorneys representing Fairholme with respect to its investments in Fannie Mae and Freddie Mac. All lines may be muted to prevent background noise from compromising sound quality.

After the call, a transcript will be made available on www.fairholmefunds.com.

Daniel Schmerin: Good morning, I'm Daniel Schmerin, Director of Investment Research at Fairholme. I'd like to welcome shareholders of The Fairholme Fund, The Fairholme Focused Income Fund (the "Income Fund"), and The Fairholme Allocation Fund (the "Allocation Fund" and, collectively, the "Funds"), and other listeners to today's 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, who will offer some opening remarks.

Bruce Berkowitz: Thanks, Dan, and good morning to everyone. It's a pleasure to be hosting this call today. I want to highlight a few points before we turn to shareholder questions. First, year-to-date performance is positive for all of our Funds and they're outpacing their respective indices with The Fairholme Fund up 13.5%, the smaller Allocation Fund up 9.5%, and our Income Fund up 22.5%, the result of a particularly strong year for income producing securities that we own in the Income Fund.

Second, I want to remind shareholders that our goal at Fairholme has always been to achieve long-term outperformance while minimizing the risk of permanent loss of capital. That remains true today. We don't try to predict uncertain futures, but rather price securities for a wide range of potential outcomes. When we're unable to disprove our highest conviction ideas, expect us to add to positions when prices drop, much in the same way you would expect us to sell when prices rise above our estimate of intrinsic value.

Third, the composition of our portfolios today reflects our view of general market values. A prolonged period of low interest rates has pushed prices of many securities sky high, and unlike most index funds, we sleep better at night knowing that we are focused on investing in true bargains. We have also recalibrated the portfolio to take advantage of select credit opportunities where we can generate equity-like returns from more senior securities that companies wish to repurchase.

And we have maintained cash for liquidity irrespective of market conditions.

Overall, our special situation investments have significantly less correlation with interest rate and equity market indices. I believe the Funds have the wherewithal for outsized rewards while protecting against the inevitable headwinds caused by rising interest rates and high valuation levels. We are more than ready for bear and bull.

Now I want to make sure we address the key points of 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 September of this year, a Morningstar analyst raised questions about the liquidity and concentration of certain investments in The Fairholme Fund. Bruce, how would you respond?

Bruce Berkowitz: Well, let's back up a little bit. Five years ago, Morningstar thought I was a hero, the "Fund Manager of the Decade."[1] Today, they apparently think I'm a zero. Everyone's entitled to their own views and time will tell. As I noted in my Semi-Annual Report[2] a few months ago, I believe the Funds have more than necessary liquidity. Liquidity is a metric we have always monitored very carefully, and today is no different. We have substantial dry powder for tomorrow's opportunities. Our commercial paper program is generating over one percent per annum with a duration of under six days, and it's focused on the companies that we know. We're not cutting any corners. We're mindful of every single dollar in the Funds.

With respect to our fixed income investments in the Funds, our positions are much more liquid than many market pundits assumed. In fact, there are a number of issuers within the Funds that are buying back their own debt, and they're publicly stating a desire to buy back their securities in a similar fashion to our historical experience with American International Group (AIG) and General Growth Properties (GGP).

Daniel Schmerin: Some shareholders noted your commentary earlier this year about a shift toward income-producing securities. With respect to The Fairholme Fund, can you shed light on the portfolio's current composition? What percentage is common stocks and what percentage is in fixed income?

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[1] **Domestic Equity Fund Manager of the Decade (2000-2009)**: The Morningstar Fund Manager of the Decade award, which was awarded for the first time in 2010, recognizes fund managers who have achieved superior risk-adjusted results over the past 10 years and have an established record of serving shareholders well. While the awards focus on performance over the past decade, Morningstar takes into consideration other factors, including the fund manager's strategy, approach to risk, size of the fund, and stewardship. Both individual fund managers and management teams are eligible, and being a previous winner of the Morningstar Fund Manager of the Year award isn't a prerequisite. Morningstar's fund analysts select the Fund Manager of the Decade award winners based on Morningstar's proprietary research and in-depth evaluation.

[2] *Fairholme Funds, Inc. 2016 Semi Annual Report* www.fairholmefundsinc.com/Reports/Funds2016SemiAnnual.pdf

Bruce Berkowitz: Dan, approximately 30% of The Fairholme Fund is invested in common stocks. Roughly 25% of The Fairholme Fund is invested in preferred stocks. Combined, that's about 55% in equity positions. Another 25% of The Fairholme Fund is in corporate bonds, and the remaining 20% is in cash and cash-equivalents, including investment grade commercial paper rolling off every day. So, The Fairholme Fund is well balanced and focused on our very best ideas, just as our shareholders expect and have always expected.

In fact, all of the Funds are generating good income while we wait for targeted catalysts for each core equity and debt investment.

Daniel Schmerin: Before we discuss some of those position-specific catalysts, I'd like you to address the questions we received pertaining to tax distributions from the Funds. As we approach year-end, can you provide a sense of what shareholders should expect in 2016 in terms of tax distributions?

Bruce Berkowitz: Fairholme's CFO, Wayne Kellner, posted potential tax distributions to the Funds' website last night. I encourage shareholders to review those estimates online at www.fairholmefunds.com. We anticipate that The Fairholme Fund will have a distribution this year of under $2 per share, which is considerably less than what we experienced last year.

Daniel Schmerin: Let's turn to specific positions. The most questions we received by far had to do with the two largest financial institutions in the country: Fannie Mae and Freddie Mac. Both recently reported third quarter results. Do you still find the underlying economics of their businesses attractive?

Bruce Berkowitz: Attractive? These are two of the best businesses in America. Period. Together, they earn $30 billion on a combined basis each year. $30 billion. Attractive? Attractive is an understatement. Fannie Mae's CEO just stated that their underlying fundamentals are strong and they expect to remain profitable for the foreseeable future.[3] The average FICO score – and FICO score is a measure of borrower quality – for Fannie Mae's single family book of business is 745, and delinquencies have dropped for 26 consecutive quarters. Really, how do you spell "pristine"? The same is true for Freddie Mac. Freddie Mac's CEO emphasized earlier this month that the company is stronger than ever with credit quality at its best in eight years.[4]

Fannie Mae and Freddie Mac are insurance companies. Fannie Mae and Freddie Mac are not banks. Fannie Mae and Freddie Mac insure and ensure affordable, predictable mortgages. Fannie Mae and Freddie Mac provide a unique, vital service that enables American families to achieve the American dream. Fannie Mae and Freddie Mac are phenomenally strong and they are sustainably profitable. Their social good and economic value is world class. This is obvious to anyone who just counts the cash Fannie Mae and Freddie Mac generate.

And it's obvious that Fannie Mae and Freddie Mac are as solid as any financial enterprise in the world, public or private. Yet, the companies are priced for less than runoff liquidation.

Daniel Schmerin: So where do we go from here?

Bruce Berkowitz: I'm going to let David Thompson of Cooper & Kirk address our progress in the courts of law. But first, I want to remind our shareholders of the following. In early 2014, I wrote that many believed Fannie Mae and Freddie Mac would be victims of a government sponsored expropriation that brings our country closer to a future such as that conceived by George Orwell in his novel, *1984*. Conventional wisdom was that the companies would be liquidated. Of course, we disagreed. Our investment in Fannie Mae and Freddie Mac was predicated on a simple thesis: There are no substitutes. Fannie Mae and Freddie

[3] "Third Quarter 2016 Earnings Media Call" Remarks Adapted from Comments Delivered by Timothy J. Mayopoulos, President and CEO of Fannie Mae, November 3, 2016, http://www.fanniemae.com/portal/media/speeches/2016/speech-mayopoulos-q32016.html.

[4] Layton, Donald H., "Freddie Mac Reports Another Quarter of Solid Financial Results," November 1, 2016, http://www.freddiemac.com/news/blog/donald_layton/20161101_financial_results_3q2016.html.

Mac are the largest providers of liquidity to our mortgage markets. The financial services they provide benefit American renters, buyers, and existing homeowners in both good and bad times. Fannie Mae and Freddie Mac *are* the housing finance system in America, and they earn a nominal amount – less than 40 basis points – for ensuring that the venerable 30-year fixed-rate mortgage remains widely accessible and affordable, especially when every bank in the country refuses to do so without their support.

Fairholme applauds their social good, which has helped tens of millions of families have a home and build retirement nest eggs. We're not arrogant. We're not telling our government or the people of our country what to do. But, we do have common sense solutions that would result in big wins for the country. Fannie Mae and Freddie Mac should transform into low-risk, public utilities with regulated rates of return, just like everyone's local electric companies.

Any intellectually honest observer will admit that the rational next step is to halt the payment of any further monies to the United States Treasury ("Treasury"), permit the companies to retain capital in order to protect tax-payers, and eventually release them from the shackles of a perpetual conservatorship.

Only the disingenuous would assert that recapitalization of these companies would take decades and come at taxpayers' expense, as if retaining earnings precluded the ability of each company to raise equity from private investors.

Only those beholden to special interests would ignore the substantial reforms implemented at Fannie Mae and Freddie Mac over the last eight years and pretend the companies are somehow doomed to repeat the past upon release from conservatorship.

And, really, only those who oppose the dream of American homeownership would attempt to dismantle two publicly traded, shareholder-owned companies that have singlehandedly provided $7 trillion – yes, trillion – in liquidity to support America's mortgage market since 2009.

With a new administration coming into office, we're quite optimistic that the indispensability of these two companies to affordable homeownership eventually overpowers the taboo imposed upon them by the conventional Washington establishment.

That being said, we're fighting in the courts to protect our shareholders' assets. Our shareholders have paid hard earned cash in exchange for contracts executed with Fannie Mae and Freddie Mac. Fannie Mae and Freddie Mac are obligated to protect the capital of all preferred shareholders, not just one of those shareholders – the Obama Treasury. Fannie Mae and Freddie Mac are obligated to obey the laws of our great country, laws that every investor, small and large, depends on each day in our financial market.

Daniel Schmerin: David, we received many shareholder questions pertaining to our ongoing litigation, particularly what we are expecting, when we are expecting it, and the magnitude of those potential outcomes. So can you start by providing our shareholders with an update of our ongoing case in the U.S. Court of Appeals for the District of Columbia Circuit (the "D.C. Circuit")?

David Thompson: Certainly, I'd be happy to, Dan. With respect to timing, there was an oral argument held on April 15 of this year. The D.C. Circuit has an informal term, so they hear cases from September to May. From September of 2015 through May of 2016 they heard 308 cases, and 304 of those cases have now been decided. We and three other litigants are still awaiting our decision, so we should be close. They release their opinions on Tuesdays and Fridays between 10:00 a.m. and noon.

In terms of why it's taking so long, we think the most reasonable and plausible explanation is the fact that there's probably a dissent being written. I think that anyone who listened to that oral argument, which is available online on the court's website, would understand that there seemed to be a difference of opinion.[5] Fortunately, two of the judges seemed favorably inclined to our view, and, in particular, we're really looking at six key issues. If we win on any of these six key issues, it will result in a tremendous victory for Fairholme.

Number one is the question of whether the Federal Housing Finance Agency ("FHFA") acted as a genuine conservator. As such, the FHFA is required to preserve and conserve assets, and is required to operate the entities in a sound and solvent manner. Clearly, not having a nickel of capital on the balance sheet, sending the entirety of the net worth, quarter after quarter, to the federal Treasury, is not sound.

And, we were very gratified when Judge Douglas Ginsburg, one of the three members of the panel, said it was "clearly true" that you could not be sound and solvent if you are giving every nickel of capital away quarter after quarter. Moreover, he noted that by imposing the Net Worth Sweep, the Treasury essentially said: "We are going to kill the companies, drive a stake through their hearts, we're going to salt the earth, so they can never grow back."[6]

Given that the statute requires rehabilitation, driving a stake through the heart of the companies and salting the earth is obviously the opposite – the antithesis – of soundness, solvency, preserving, conserving, rehabilitating … all of the things that the statute requires.

Now, the government has tried to defend its conduct by saying that the companies were in a death spiral, that they couldn't meet their dividend obligations. We know that's nonsense because we can see the massive profits that the companies have generated over the last four years.

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[5] *Perry Capital LLC v. Jacob Lew*, https://www.cadc.uscourts.gov/recordings/recordings2016.nsf/74B30C9776477AA885257F96006585FE/$file/14-5243.mp3

[6] *Perry Capital LLC v. Jacob Lew*, https://www.cadc.uscourts.gov/recordings/recordings2016.nsf/74B30C9776477AA885257F96006585FE/$file/14-5243.mp3

In fact, the government itself knew it was nonsense because Susan McFarland, the CFO of Fannie Mae, has testified in her deposition that on the eve of the Net Worth Sweep, she went in and met with high ranking Treasury officials and she, in fact, told them to their face that Fannie Mae was going to make massive profits in 2013. So the government was, in fact, on notice of this reality.

That's one of our six key issues. I'll go through the others more quickly.

We've got an argument that Treasury directed and imposed the Net Worth Sweep. The Housing and Economic Recovery Act of 2008 ("HERA"), the governing statute, forbids that. FHFA is not permitted to act at the direction or supervision of any agency, including Treasury.

Our third issue is that Treasury itself exceeded its own authority by purchasing a new security after the time that it was permitted to do so. It was only allowed to purchase new securities through December 31, 2009. Of course, the Net Worth Sweep was enacted in August of 2012. We have revenue rulings from the Treasury itself indicating that this type of change from a fixed-rate preferred security to something that is akin to common stock is, in fact, a new security. Therefore, this would constitute a purchase.

Fourth, we have a breach of fiduciary duty claim. Obviously, the sort of incredible self-dealing transaction in which massive amounts of net worth are expropriated in return for essentially no consideration would be a classic example of a breach of fiduciary duty.

Fifth, we have our breach of contract claim. As preferred shareholders, we have a right not only to a liquidation preference, but also to a dividend stopper. No dividends can be paid on common stock if our contracts are not being honored and if our dividends are not being paid. That's exactly what's happening here now that the Treasury essentially has common and is paying itself dividends.

And, number six is the breach of the implied covenant of good faith and fair dealing. Obviously, no one would have ever given Fannie Mae and Freddie Mac the $33 billion that it raised through preferred stock offerings if they had realized that the companies had the ability and the authority to just give the money to an affiliated entity and violate the contracts that way.

So, those are our six key issues, and we feel very good that we are right and we should prevail on these issues.

Daniel Schmerin: So, does purpose and effect matter? In other words, is motive irrelevant in this instance?

David Thompson: Well, the government obviously wants to make motive irrelevant because, as I just indicated, they, in fact, knew that when they did this they were going to be taking tens of billions of dollars in the biggest expropriation of private property in the history of the United States of America. So, they would like to have the courts blind themselves to the purpose. We say that's wrong, and that the statute itself includes and brings in the concept of purpose and that FHFA is limited by having a proper and legitimate purpose.

But, we also say that even if the government were right, and the courts were to blind themselves to purpose, you'd have to look at effect then. And, the effect is that these companies are not being operated in a sound profile. They are having all of their net worth stripped out of them. There is not a single financial institution in the United States, let alone the two biggest, that is allowed to operate with zero capital. That is the antithesis of soundness, and that is the effect of what the government has done here.

Daniel Schmerin: One of the six issues you mentioned was the breach of contract claim. So, can you just explain to shareholders what our recovery would look like if we were to prevail on the breach of contract?

David Thompson: Yes, there are three standard remedies for a breach of contract.

One is expectancy damages, which puts us in the position that we would have been in if there had been no breach of contract. Two is reliance, which is to give us our out-of-pocket costs. The third is restitution. We're entitled to present evidence of all three and pick the highest.

But, I want to focus on restitution, because I think that is really the concept that is the most relevant here, and it's pretty simple. You look at the benefits that the breaching party received – and here the breaching party would be Fannie Mae and Freddie Mac – and the benefit they received was par value, $25 a share. From that, you would potentially subtract any benefits as they would probably argue for an offset of any dividends that the preferred shareholders received. Now as we know, two thirds of this float was issued in 2007 and 2008. So, for those series the offset from par value would be somewhere between zero and five dollars a share. Thus, we could be looking at damages of $20 a share if we are successful on our breach of contract claim and the court agrees with us about restitution.[7]

Daniel Schmerin: Can you provide shareholders with an update on our case before the U.S. Court of Federal Claims? Since the government has effectively nationalized Fannie Mae and Freddie Mac, isn't the merit of that case rather obvious?

David Thompson: Well, we certainly think so. As I indicated, it's the largest and most egregious taking of property in the history of the country, and the government has vigorously resisted our ability to look into its internal discussions and to get to the truth of the matter as to why they did this. They have also resisted making any of this information public, and now we know why. As I indicated a moment ago, once we got an opportunity to see certain internal e-mails, once we were able to depose the key officials, we were able to determine that their death spiral narrative – the notion that Fannie and Freddie weren't going

[7] For the sake of brevity, a discussion on penalty interest and its calculation was omitted from the answer.

to make enough money to pay dividends – was absolutely ridiculous. And, in fact, the Treasury Department knew as much.

In addition, what the government has done is they have tried to draw an iron curtain around many of their deliberations. They have asserted privilege over somewhere between 11,000 and 12,000 documents, roughly 100,000 pages. This is the mother of all privilege logs, and they are clearly overreaching. They even assorted privilege over e-mails with outside private parties – clearly not privileged. We were forced to go to court to contest their broad assertion of privilege. We picked 56 documents that we thought were a representative sample of the 11,000 plus documents and Judge Margaret Sweeney issued an 81-page single spaced opinion in which she determined that all 56 documents should have been turned over to us.

So we went 56 for 56. Now, rather than giving us those documents, the government has filed an emergency appeal with the Federal Circuit using a mechanism called mandamus, which is an extraordinary mechanism, arguing that we shouldn't be entitled, that we don't need these documents, and that they don't need to give them over. Obviously, we think Judge Sweeney's opinion is meticulous, thoroughgoing, and followed the law very carefully. So, we are very confident that we are going to win on mandamus. And in those 56 documents are memos to the President to the United States. We are very interested to see whether the President knew the truth or was being misled himself by his subordinates. So, we believe there are some important documents in there – but we haven't seen them yet. We are eager to continue on with that discovery process.

Daniel Schmerin: Is it accurate then to describe the government's strategy as deny and delay?

David Thompson: Yes, absolutely. They are trying to drag this out as effectively as they can, number one. And, they are trying to deny us access to the truth at every step of the way. In my experience as a litigator, when you've got a party who is consistently denying you access to the relevant factual information, that normally is an indication that there is something there that is damaging to their case. We've been very gratified that, thus far, Judge Sweeney has been very vigilant about not allowing the government to deny us access to the truth.

Daniel Schmerin: Is there any reason to believe that a Trump Administration will continue this administration's blatant attempt to hide incriminating evidence from the public and courts of law?

David Thompson: It's still early, but we're certainly optimistic that the Trump Administration would take a different approach. We think it's unlikely that they would perpetuate the same sorts of tactics of deny and delay that we are seeing from the Obama Administration.

Daniel Schmerin: What about some of the other cases that are pending in places like Iowa, Illinois, Texas, and even Delaware?

David Thompson: Those cases are largely in a holding pattern as everyone is waiting on guidance from the D.C. Circuit. The D.C. Circuit decision won't be binding on these other courts, but obviously it's an extremely well respected court, and everyone is eager to see what the court has to say.

I think the Texas suit that you referenced is particularly interesting because it has a new claim that is not in any of the other suits. It's a claim that isn't correlated with any other litigation, and it's a claim that doesn't depend on any facts whatsoever. It is a claim that the FHFA is itself unconstitutional, and this theory grows out of an opinion issued by the D.C. Circuit earlier this year by an extremely well respected judge, Brett Kavanaugh, who did an extremely detailed opinion relating to the Consumer Financial Protection Bureau ("CFPB"), saying that it was unconstitutional to have an independent agency with a single head.

And, in that opinion, Judge Kavanaugh pointed out that the CFPB isn't the only agency that is vulnerable to this sort of attack. The FHFA is, too. So, that Texas suit includes that count, and it's very interesting. If it were successful, then the Net Worth Sweep would be vacated. I think that all of those suits are important to look at, but certainly Texas is as well.

Daniel Schmerin: From a legal perspective, how would you characterize the differences between the preferred stock that we own and common stock owned by other Fannie Mae and Freddie Mac shareholders?

David Thompson: Well, of course, the preferred stock is more senior in the capital structure. Also, the preferred shareholders have a contract right to, (A) a liquidation preference, and (B) a dividend stopper. As I indicated, under the terms of the contract, Fannie Mae and Freddie Mac are not permitted to pay dividends to common stockholders unless they have paid dividends to the preferred. So that's an important distinction and candidly, if the common stock is worth a penny, then Fairholme's preferred should be money good.

David Schmerin: Given that you're based up in Washington, D.C., have you sensed a shift in sentiment regarding Fannie Mae and Freddie Mac?

David Thompson: I really think there is a shift in sentiment. I think there has been a sea change. We were hearing several years ago that they are a failed business model, that when they lose money, they hand the bill to the taxpayers and when they make money it goes to the private sector. That's absolutely false. It's not a failed business model. As Bruce was indicating earlier, they are phenomenally profitable. They paid the government back every penny plus tens of billions of dollars in profits in return. So, the notion that they are a failed business model, that narrative, we're just not hearing it anymore.

In addition, we're beginning to see a recognition that this Net Worth Sweep, now that that capital is being whittled down to zero, is just not tenable. Mel Watt, in a speech earlier this year, said, "The most serious risk and the one that has the most potential for escalating in the future is the enterprise's lack of capital."[8] That's exactly what we're saying in our lawsuit, and it's very telling that here we have the head of the defendant agency acknowledging as much.

Also of significant interest was an article in the *Washington Post* written by Tom Forrester, a former board member of Fannie Mae who served from December of 2008 to May of 2016. In this *Washington Post* article he writes, quote, "I can tell you that stripping the firms of their profits and their capital poses a huge risk."[9]

That's obviously self-evident to anyone who's familiar with financial institutions, but it's a big change here in Washington because people wanted to ignore that huge risk, the government is asking the courts to blind themselves to the huge risk, and I think it's very telling that policymakers, a member of the board of Fannie Mae, and even the defendants themselves are recognizing that capital is key.

Daniel Schmerin: So tell us what comes next. How feasible is a negotiated settlement?

David Thompson: Well, we're in regular communication with the Department of Justice. They are aware of our willingness to resolve the ongoing litigation in a prompt manner. But make no mistake, we are prepared to see this matter through and we remain very confident that we will prevail.

Daniel Schmerin: Fairholme shareholders know that our motto is "Ignore the crowd." Does Cooper & Kirk have a motto of its own?

David Thompson: Well, we do. It's "*vincere aut mori*." That's Latin for "victory or death." All of us have a large six-foot sword in our offices to remind

[8] Watt, Melvin L., "Prepared Remarks of Melvin L. Watt Director of FHFA at the Bipartisan Policy Center," February 18, 2016, http://www.fhfa.gov/Media/PublicAffairs/Pages/Prepared-Remarks-Melvin-Watt-at-BPC.aspx.
[9] Forrester, Tom, "Is it time to start worrying about Fannie Mae and Freddie Mac again?" *Washington Post*, October 28, 2016, https://www.washingtonpost.com/business/is-it-time-to-start-panicking-about-fannie-mae-and-freddie-mac-again/2016/10/28/e05e609a-9016-11e6-a6a3-d50061aa9fae_story.html.

us every day of that motto. And let me emphasize in the strongest possible terms: we fully intend to win this fight.

Daniel Schmerin: Thank you, David. Bruce, let's pivot to some of the other positions in our portfolio, such as the St. Joe Company ("St. Joe"). The name first appeared in The Fairholme Fund portfolio back in 2008. Performance has been rather unremarkable since then. Why should shareholders believe that will change?

Bruce Berkowitz: Well, I'm going to answer that question, Dan. But before that, I've got to say thank you, David. I am very excited about the work David and his team have done at Cooper & Kirk. They've done a great job.

David Thompson: It's been an honor, Bruce, thank you.

Bruce Berkowitz: Thank you, David. On to St. Joe. I think basically that the facts on the ground at St. Joe are flashing positive. I recognize that the pace of play at St. Joe has been slower than we would have hoped for, but I am excited. First of all, I'd like to remind our shareholders that I serve as the chairman of St. Joe and that Fairholme and our affiliates own about one-third of the company.

That being said, here's our analysis. St. Joe is well capitalized, it's entitled to develop 170,000 residential units and 22 million square feet of retail, commercial, and industrial facilities on 110,500 acres of nearly contiguous land on Florida's emerald coast. St. Joe's management is very focused on growing recurring revenues while maintaining a low fixed expense structure. St. Joe is seeing an increase in housing absorption around Panama City and Walton counties, and creating more demand for finished lots.

St. Joe's commercial properties, such as Pier Park North, are experiencing high levels of occupancy and foot traffic. Eastern Shipbuilding, one of St. Joe's tenants at Port St. Joe, recently won the largest contract in U.S. Coast Guard history to build a new fleet of Coast Guard cutters. This $10.5 billion contract is transformative for Northwest Florida.

And more business begets more jobs, which requires more skilled workers, which leads to more residential demand, which, in turn, leads to greater commercial activities. It's a virtuous circle. And St. Joe is scaling this virtuous circle by building densities in all of its core areas. St. Joe's pipeline of potential residential and commercial projects has never been better. And St. Joe has immense liquidity and flexibility to achieve the goal.

To our shareholders, I say, "Stay tuned." And don't forget that owning hard assets in what I believe will be an inflationary environment down the road can prove to be very profitable.

While the progress at St. Joe is steadily growing, I hope our shareholders recognize that when it comes to certain investments, it can take years to become an overnight success.

Daniel Schmerin: Imperial Metals Corporation ("Imperial Metals") reported its third quarter results just a few days ago. What are the key risks and potential opportunities associated with his position?

Bruce Berkowitz: Well, metal and mining companies invariably experience cyclical stress and price fluctuations, and Imperial Metals is no exception. However, I believe Imperial Metals has world class assets and a highly capable management team that can successfully execute on their long term plans to unlock the value of one of the earth's largest copper and gold deposits.

We first bought Imperial Metals after observing Murray Edwards develop Canadian Natural Resources, particularly its massive Horizon Oil Sands ("Horizon") project, into a top-tier energy producer. We believe that Imperial Metals' Red Chris mine is a replay of low-cost Horizon, but with one of the largest copper resources and the seventh largest gold deposit in the world.

It's important to maintain a perspective about a project like Red Chris, which has the capability to produce copper and gold at double the current production rates for the next 100 years. By all accounts, it is a huge resource and we expect that it will prove very profitable for shareholders over time. That is the opportunity that Imperial Metals presents.

As far as key risks, we've unfortunately experienced a number of them over the last few years. For instance, an unexpected breach at Mount Polley's tailings facility has cost the company much time and money. And declines in copper prices have reduced margins at precisely the point when Imperial Metals was commencing operations at their flagship Red Chris. And, any time you launch a major new project there are inevitably some growing pains. We see that today in the recovery rates reported in Imperial Metals' latest quarterly report. Recovery rates are about 10 percentage points lower than anticipated.

But at the end of the day, Imperial Metals has been able to achieve mill-specification processing rates in record time, and Red Chris copper equivalent cash costs are lower than 75% of all other copper mines in the world. Management is intensely focused on improving recovery rates in the months ahead. Patience should really pay with this one.

Daniel Schmerin: How is Chesapeake Energy ("Chesapeake") handling the low commodity price environment? And, can you provide an update on our investment in Chesapeake's senior bonds?

Bruce Berkowitz: Well, new management at Chesapeake has done a great job ensuring that all financial obligations are being met amidst the downturn in oil and gas prices. They have reduced near term maturities by approximately $3 billion, which provides them with a solid runway to execute their business plan. They've reduced total debt by $1.5 billion via open market purchases, tenders, exchanges, and debt-for-equity swaps.

They've cut deals with Williams Partners, LP to fix legacy gathering contacts in various basins, further driving down the company's cost structure. They are laser focused on increasing cash flow through more efficient drilling and select asset sales, which should reach about $2 billion this year. So they're being very prudent and very proactive, and the value of Chesapeake's enormous asset base, combined with management's financial and operational activities, cement our view that the debt investments that we hold in the Funds are money good.

Daniel Schmerin: Many shareholders submitted questions about Sears Holdings Corporation ("Sears"). And while folks acknowledge that you joined the Board of Directors earlier this year and have some limitations on what you can discuss publicly, I want us to touch on a few issues that repeatedly came up. First, why are you sticking with Sears? Isn't this a melting ice cube?

Bruce Berkowitz: We're sticking with Sears because of our valuations regarding net assets. When we first started investing in Sears, we estimated net assets of over $250 per share. Over time, due to cash burn and corporate distributions, those estimates have been reduced to $150 per share. These are independent estimates that Fairholme has backed up with independent analysis from various professional firms.

We believe tremendous value still exists at Sears based upon the net assets within the company. And given the current stock price, we can do nothing but wait. We are excited. The difference is dramatic. The margin of safety is dramatic, and we expect to see those net asset values eventually reflected in the market price of Sears.

Daniel Schmerin: What is Fairholme's ownership across Sears' capital structure?

Bruce Berkowitz: Accounting for all of Fairholme's clients, we own about 26% of the common stock of Sears. We own about 31% of all the outstanding warrants to purchase Sears common stock. We own about 15.5% of the senior secured notes due in 2018. And we own over 57% of the senior unsecured notes due in 2019. There's no sugar coating it. We own a substantial stake across Sears' entire capital structure, and we absolutely expect that these investments will prove very lucrative for all of our shareholders in due course.

Daniel Schmerin: Some shareholders wanted to know why we aren't buying more Sears common stock at today's lows.

Bruce Berkowitz: It's pretty simple. Being on the board restricts my actions at certain times.

Daniel Schmerin: What is the worst-case scenario for our investment in Sears? What does your "kill the company" analysis reveal?

Bruce Berkowitz: The worst-case scenario is that our estimated net asset values of the company continue to decline toward current market prices.

Daniel Schmerin: Does Sears have a plan to eliminate the ongoing cash burn?

Bruce Berkowitz: On this topic, I defer to CEO Eddie Lampert who has written in detail on the plans to halt cash losses while optimizing asset values. I recommend all of our shareholders read his annual letters.

Daniel Schmerin: How does the rising popularity of online shopping and e-commerce affect Sears' large brick and mortar footprint?

Bruce Berkowitz: It's clear that what we call "shoppertainment" is only growing. Online and in-store shopping go hand-in-hand. And shopping centers remain community meeting places – places to physically interact and entertain. When you correctly broaden the definition of retail to include what we call "shoppertainment," the definition of that ecosystem is quite clear and quite healthy.

Daniel Schmerin: Under what conditions would you sell your stake in Sears?

Bruce Berkowitz: I get this question all the time, and it's no different than when we would sell a position in any company. When the market price exceeds our intrinsic value estimate, we're sellers.

Daniel Schmerin: Let's turn to Seritage Growth Properties ("Seritage"), which was spun off from Sears in mid-2015. Are you satisfied with the progress at Seritage?

Bruce Berkowitz: Yes. Seritage is transforming retail rents from $4 per square foot to $20 plus. I believe, in fact, that the parking lots associated with the retail spaces may even prove more valuable than those retail spaces. Any way you slice it, on an enterprise value per square foot basis, Seritage is a great investment.

I recommend that shareholders look at the latest presentation released by the company to get a taste of the redevelopment projects underway in places like Charleston, South Carolina; Springfield, Illinois; West Hartford, Connecticut; as well as renderings of large projects in Santa Monica, California, and Redmond, Washington, to name just a few. The latest presentation went up earlier this week. A very important fact is that Seritage clearly proves the point about the value of the real estate remaining at Sears.

Daniel Schmerin: Bruce, our final question: back in February you teased that your mother had fired you yet again. Shareholders asked, "has she returned to her senses, and where does she stand today?"

Bruce Berkowitz: Well, Dan, she last threatened to buy an index fund. Luckily, her bouts of irrationality last less than 24 hours. I'm proud to report that she remains a loyal client. Kidding aside, long-term shareholders know very well that my family is fully invested in Fairholme ideas. That has always been the case, and that will always remain the case.

Daniel Schmerin: Good to hear. 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: To all our shareholders, thank you. Thank you for your trust, thank you for your confidence. We're going to prove to you that Jean-Jacques Rousseau had it right when he said, "Patience is bitter, but its fruit is sweet." We are working 24/7 to move shareholders onward and upward.

Operator: Thank you 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 http://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.

The Fairholme Focused Income Fund (the "Income Fund") is a non-diversified mutual fund, which means that the Income Fund invests in a smaller number of securities when compared to more diversified funds. This strategy exposes the Income Fund and its shareholders to greater risk of loss from adverse developments affecting portfolio companies. The Income Fund's investments are also subject to interest rate risk, which is the risk that the value of a security will decline because of a change in general interest rates. Investments subject to interest rate risk will usually decrease in value when interest rates rise and rise in value when interest rates decline. Also, securities with long maturities typically experience a more pronounced change in value when interest rates change. Debt securities are subject to credit risk (potential default by the issuer). The Income Fund may invest without limit in lower-rated securities. Compared to higher-rated fixed income securities, lower-rated debt may entail greater risk of default and market volatility.

The Fairholme Allocation Fund (the "Allocation Fund") is a non-diversified mutual fund, which means that the Allocation Fund can invest in a smaller number of securities when compared to more diversified funds. The Allocation Fund may invest in lower-rated securities, which may have greater market risk. This strategy exposes The Allocation Fund and its shareholders to greater risk of loss from adverse developments affecting portfolio companies. The allocation of investments among the different asset classes, such as equity or fixed-income asset classes, may have a more significant effect on The Allocation Fund's net asset value when one of these classes is performing more poorly than others.

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 (11/16)

THE FAIRHOLME FUND

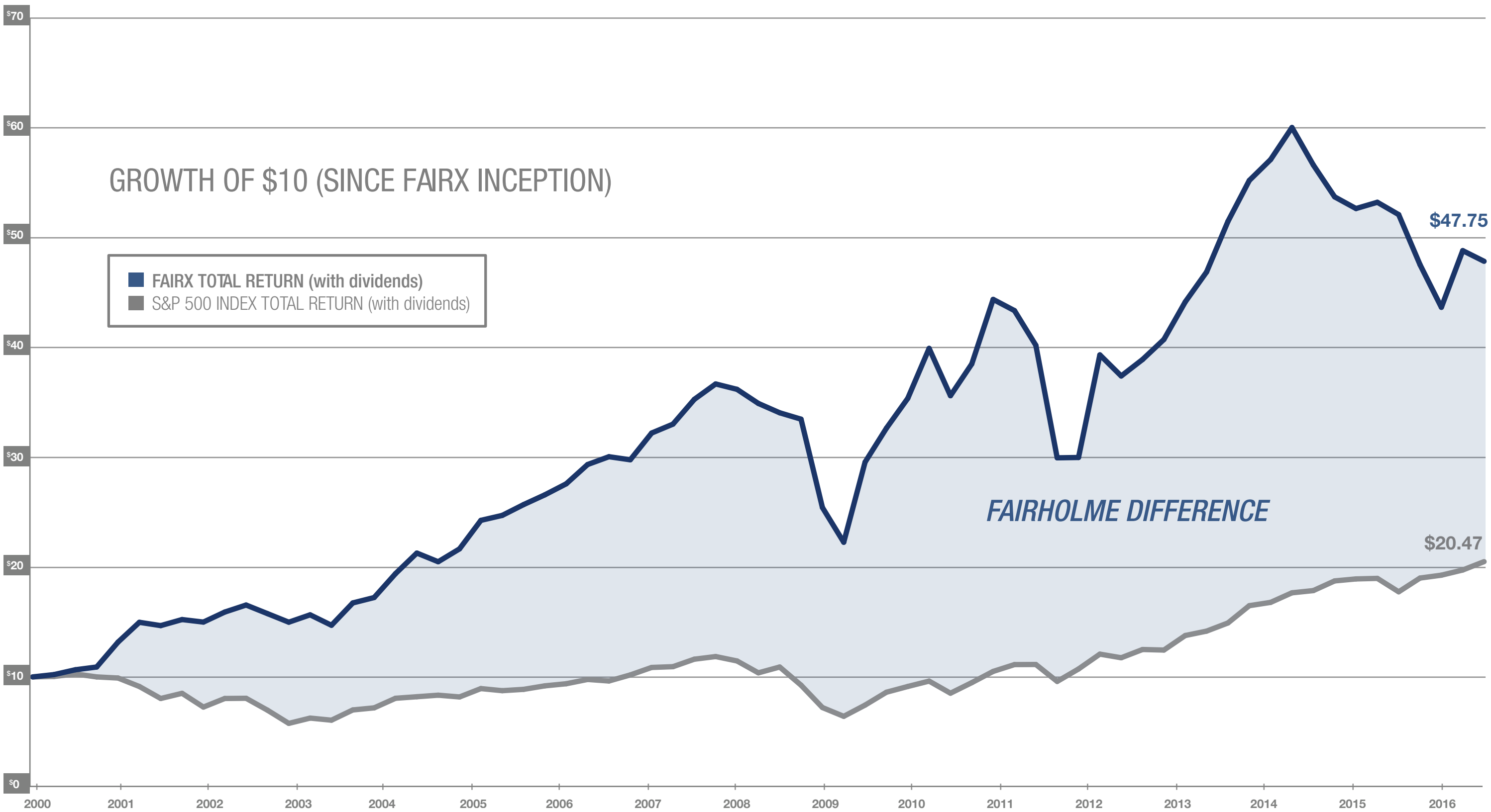
*Managed by **Bruce Berkowitz,** Chief Investment Officer of Fairholme Capital Management (the "Manager")* at 9/30/16

Seeks long-term growth of capital.

Growth of $10 (Since Inception)[1]	
Net Asset Value	$18.62
Distribution Value	$26.13
Reinvestment Value[2]	$3.00
Total Value	**$47.75**

60-Month Rolling Returns	FAIRX	S&P 500 Index
Best	+185.26% (3/2009-2/2014)	+181.57% (3/2009-2/2014)
Average	+65.86%	+40.55%
Worst	-6.89% (1/2007-12/2011)	-29.05% (3/2004-2/2009)
Percentage of Positive Periods[3]	96%	81%

Fund Manager of the Decade[4]
Domestic Equity



The chart above covers the period from inception (December 29, 1999) of The Fairholme Fund (the "Fund" or "FAIRX") to September 30, 2016. ***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 (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 the S&P 500 Index, it should be inherently less volatile. Our results may differ markedly from those of the S&P 500 Index in either up or down market trends. The performance of the S&P 500 Index 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 Fund is 1.04%. The expense ratio includes acquired fund fees and expenses which are incurred indirectly by the Fund as a result of investments in securities issued by one or more investment companies.*

Cumulative Return	FAIRX	S&P 500 Index
1-Year	-8.16%	+15.43%
3-Year	-7.04%	+37.36%
5-Year	+59.70%	+113.44%
10-Year	+60.68%	+101.14%
15-Year	+218.71%	+181.75%
Since Inception	+377.49%	+104.68%

Annualized Return	FAIRX	S&P 500 Index
1-Year	-8.16%	+15.43%
3-Year	-2.41%	+11.16%
5-Year	+9.82%	+16.37%
10-Year	+4.86%	+7.24%
15-Year	+8.03%	+7.15%
Since Inception	+9.78%	+4.37%

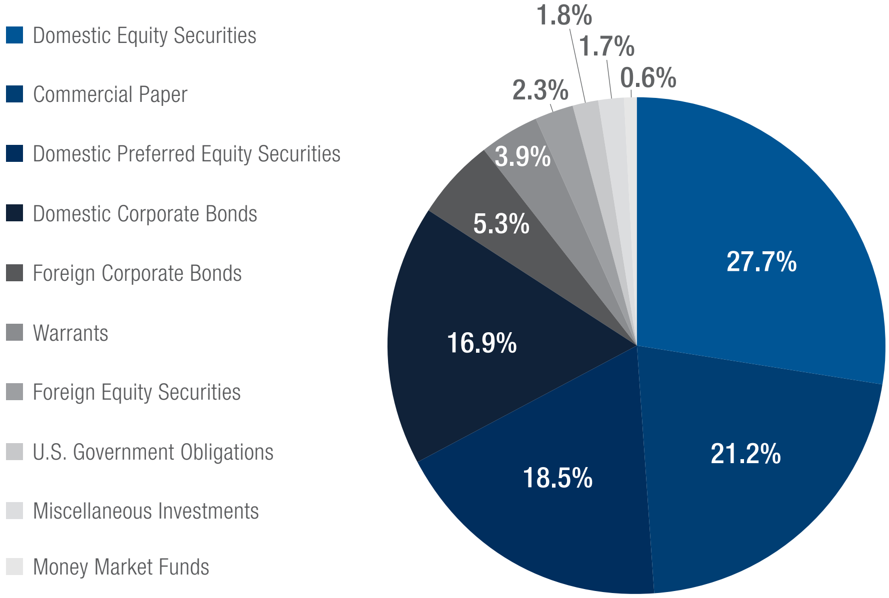
THE FAIRHOLME FUND

Top Holdings by Issuer as of 8/31/16 [5]	% FAIRX
Cash and Cash Equivalents	23.6%
The St. Joe Co.	15.8%
Sears Holdings Corp.	11.8%
Chesapeake Energy Corp.	10.8%
Federal National Mortgage Association	10.0%
Federal Home Loan Mortgage Corp.	8.5%
Imperial Metals Corp.	6.6%
Seritage Growth Properties	3.3%
American International Group, Inc.	3.2%
Lands' End, Inc.	1.5%

Investment Minimums

Initial, Regular Account[6]	$10,000
Initial, IRA[6]	$5,500
Subsequent, Regular Account and IRA	$1,000
Subsequent, Automatic Investment Plan	$250/month

Portfolio Composition by Security Type as of 8/31/16



The Fund seeks long-term growth of capital. The Manager attempts under normal circumstances, to achieve the Fund's investment objective by investing in a focused portfolio of equity and fixed-income securities. The proportion of the Fund's assets invested in each type of asset class will vary from time to time based upon the Manager's assessment of general market and economic conditions. The Fund may invest in, and may shift frequently among, asset classes and market sectors. There is no guarantee that the Fund will meet its objective.

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

(6) The minimum initial investment for regular accounts and IRAs may be waived by the Manager in its discretion.

Investing in the 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.

Shares of the Fund are not deposits or obligations of any bank, are not guaranteed by any bank, are not insured by the FDIC or any other agency, and involve investment risk, including possible loss of the principal amount invested. Automatic Investment Plans do not assure a profit and do not protect against a loss in declining markets.

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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901 K Street NW
Washington, DC 20001

The Fund's investment objective, risks, charges, and expenses should be considered carefully before investing. The prospectus contains this and other important information about the Fund, and it may be obtained by calling Shareholder Services at (866) 202-2263 or visiting our website www.fairholmefunds.com. Read it carefully before investing.

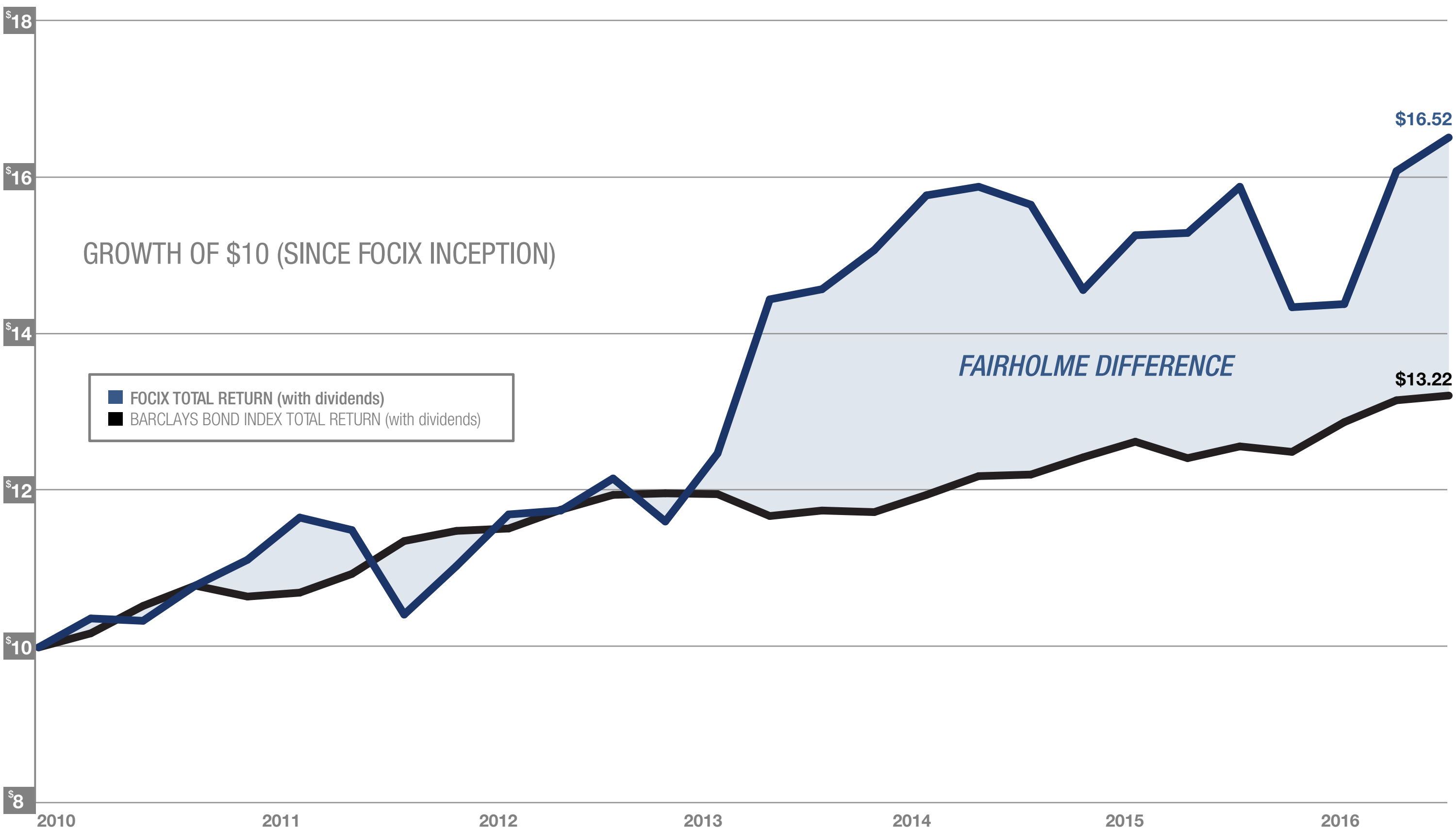
THE FAIRHOLME FOCUSED INCOME FUND

*Managed by **Bruce Berkowitz,** Chief Investment Officer of Fairholme Capital Management (the "Manager")* — at 9/30/16

Seeks current income.

Growth of $10 (Since Inception)[1]	
Net Asset Value	$10.77
Distributions	$4.55
Reinvestment Value[2]	$1.20
Total Value	**$16.52**

60-Month Rolling Returns	FOCIX	Barclays Bond Index
Best	+58.50% (8/2011-9/2016)	+25.01% (2/2010-1/2015)
Average	+42.21%	+19.39%
Worst	+17.51% (3/2011-2/2016)	+15.81% (9/2010-8/2015)
Percentage of Positive Periods[3]	100%	100%



*The chart above covers the period from inception (December 31, 2009) of The Fairholme Focused Income Fund (the "Fund" or "FOCIX") to September 30, 2016. **Performance information quoted 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 herein. Performance figures assume reinvestment of dividends and capital gains. Performance prior to March 29, 2012, reflects fee waivers by the Manager. Most recent month-end performance and answers to any questions you may have can be obtained by calling Shareholder Services at (866) 202-2263.** The Barclays Capital U.S. Aggregate Bond Index (the "Barclays Bond Index") is an unmanaged market-weighted index comprised of investment grade (rated Baa3/BBB-/BBB- or higher) taxable bonds, mortgage-backed securities, asset-backed securities, corporate securities, and government-related securities, including U.S. Treasury and government agency issues, with at least one year to maturity. It is not possible to invest directly in an unmanaged index. The Barclays Bond Index is not meant to be indicative of the Fund's performance, asset composition, or volatility. Our results may differ markedly from those of the Barclays Bond Index in either up or down market trends and interest rate environments. The performance of the Barclays Bond Index does not reflect any management fees, transaction costs, expenses, or taxes. The Fund's expense ratio is 1.01%. The expense ratio includes acquired fund fees and expenses which are incurred indirectly by the Fund as a result of investments in securities issued by one or more investment companies.*

Cumulative Return	FOCIX	Barclays Bond Index
1-Year	+3.99%	+5.19%
3-Year	+13.27%	+12.57%
5-Year	+58.50%	+16.39%
Since Inception	+65.18%	+32.24%

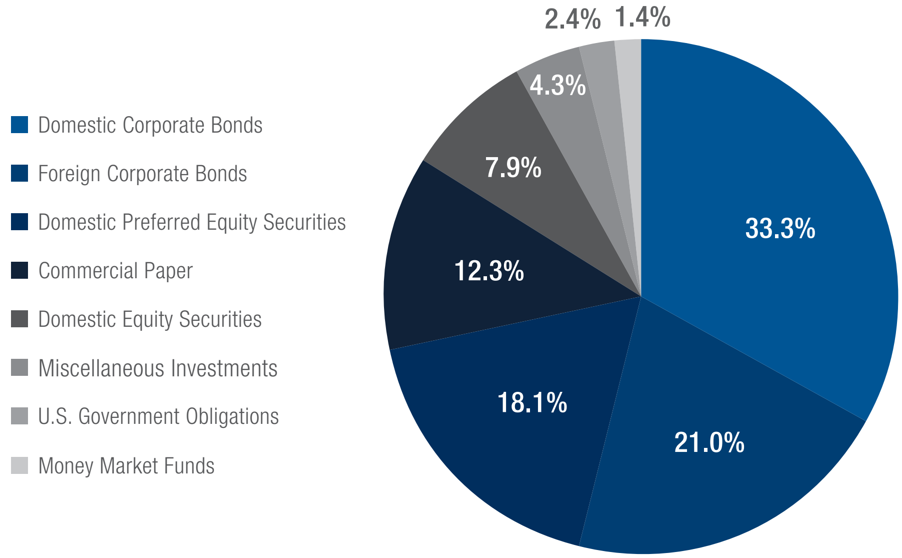
Annualized Return	FOCIX	Barclays Bond Index
1-Year	+3.99%	+5.19%
3-Year	+4.24%	+4.03%
5-Year	+9.65%	+3.08%
Since Inception	+7.71%	+4.22%

The Fund's 30-Day SEC Yield at September 30, 2016, was 6.06%.

THE **FAIRHOLME FOCUSED INCOME** FUND

Top Holdings by Issuer as of 8/31/16[4]	% FOCIX
Imperial Metals Corp.	21.0%
Cash and Cash Equivalents	16.1%
Sears Holdings Corp.	11.5%
Chesapeake Energy Corp.	9.9%
Seritage Growth Properties	7.9%
Federal National Mortgage Association	5.3%
Atwood Oceanics, Inc.	5.3%
GMAC Capital Trust I, Inc.	5.1%
Federal Home Loan Mortgage Corp.	4.8%
Homefed Corp.	4.4%

Portfolio Composition by Security Type as of 8/31/16



Investment Minimums

Initial, Regular Account[5]	$10,000
Initial, IRA[5]	$5,500
Subsequent, Regular Account and IRA	$1,000
Subsequent, Automatic Investment Plan	$250/month

The Fund seeks current income. The Manager attempts, under normal circumstances, to achieve this objective by investing in a focused portfolio of cash distributing securities. To maintain maximum flexibility, the securities in which the Fund may invest include corporate bonds and other corporate debt securities of issuers in the U.S. and foreign countries, bank debt (including bank loans and participations), government and agency debt securities of U.S. and foreign countries (including U.S. Treasury bills), convertible bonds and other convertible securities, and equity securities, including preferred and common stock, and interests in real estate investment trusts. There is no guarantee that the Fund will meet its objective.

(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 Fund.

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

(5) The minimum initial investment for regular accounts and IRAs may be waived by the Manager in its discretion.

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Shares of the Fund are not deposits or obligations of any bank, are not guaranteed by any bank, are not insured by the FDIC or any other agency, and involve investment risk, including possible loss of the principal amount invested. Automatic Investment Plans do not assure a profit and do not protect against a loss in declining markets.

The composition of the Fund's portfolio holdings and sector weightings is subject to change and should not be considered a recommendation to buy or sell any securities.

Current and future portfolio holdings are subject to risk.

Contacts

SHAREHOLDER SERVICES	MANAGER	INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM
Fairholme Funds, Inc. c/o BNY Mellon Investment Servicing (US) Inc. 4400 Computer Drive Westborough, MA 01581-1722	**Fairholme Capital Management, LLC** 4400 Biscayne Boulevard Miami, FL 33137	**Deloitte & Touche LLP** 1700 Market Street Philadelphia, PA 19103
CUSTODIAN	**DISTRIBUTOR**	**LEGAL**
The Bank of New York Mellon 225 Liberty Street New York, NY 10286	**Fairholme Distributors, LLC** 899 Cassatt Road Berwyn, PA 19312	**Seward & Kissel, LLP** 901 K Street NW Washington, DC 20001

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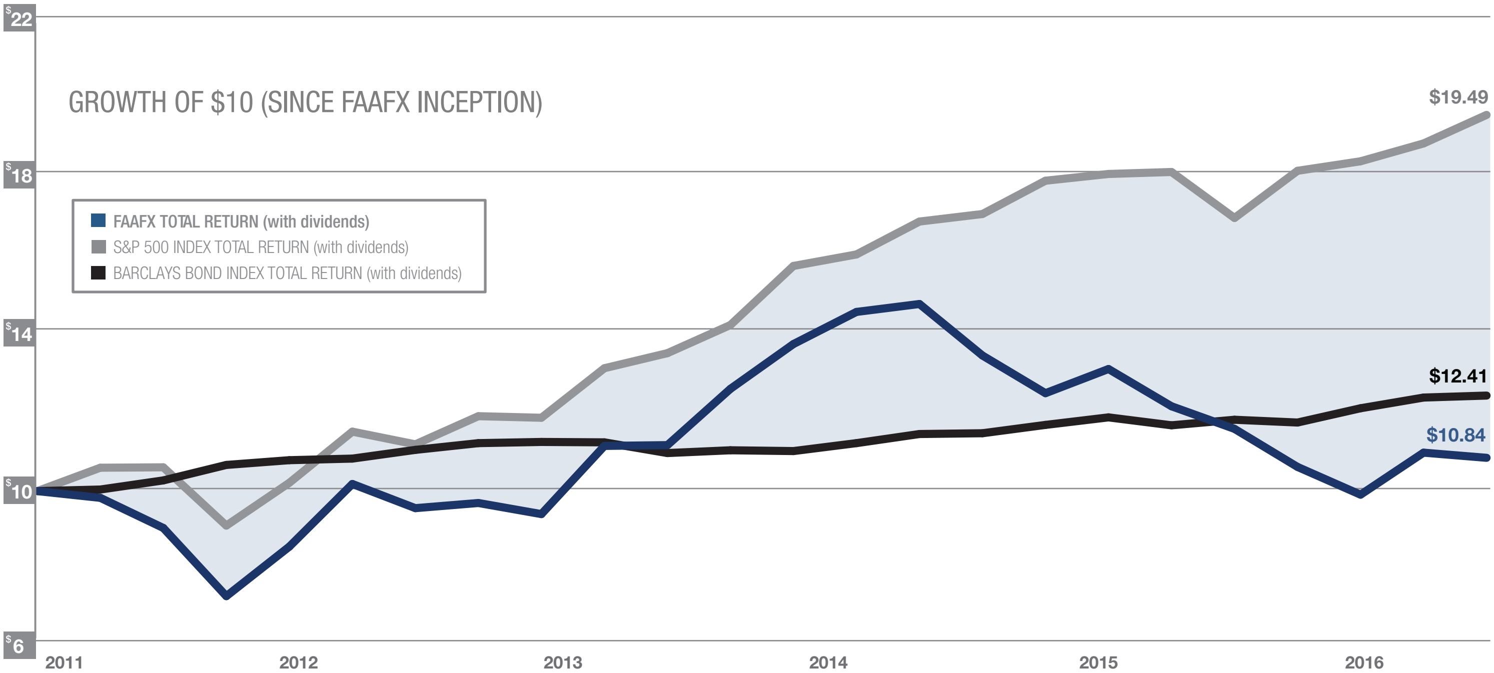
THE FAIRHOLME ALLOCATION FUND

*Managed by **Bruce Berkowitz,** Chief Investment Officer of Fairholme Capital Management (the "Manager")* *at 9/30/16*

Seeks long-term total return.

Growth of $10 (Since Inception)[1]	
Net Asset Value	$8.17
Distributions	$2.84
Reinvestment Value[2]	-$0.17
Total Value	**$10.84**

60-Month Rolling Returns	FAAFX	Barclays Bond Index	S&P 500 Index
Best	+47.48% (8/2011-9/2016)	+20.37% (4/2011-3/2016)	+113.44% (8/2011-9/2016)
Average	+15.37%	+18.61%	+80.20%
Worst	-5.91% (3/2011-2/2016)	+16.39% (8/2011-9/2016)	+62.03% (3/2011-2/2016)
Percentage of Positive Periods[3]	80%	100%	100%



*The chart above covers the period from inception (December 31, 2010) of The Fairholme Allocation Fund (the "Fund" or "FAAFX") to September 30, 2016. **Performance information quoted 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 herein. 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. Performance prior to March 29, 2012, reflects fee waivers by the Manager. Most recent month-end performance and answers to any questions you may have can be obtained by calling Shareholder Services at (866) 202-2263.** The Barclays Capital U.S. Aggregate Bond Index (the "Barclays Bond Index") is an unmanaged market-weighted index comprised of investment grade (rated Baa3/BBB-/BBB- or higher) taxable bonds, mortgage-backed securities, asset-backed securities, corporate securities, and government-related securities, including U.S. Treasury and government agency issues, with at least one year to maturity. The S&P 500 Index is a widely recognized, unmanaged index of 500 of the largest companies in the United States as measured by market capitalization, and the performance of the S&P 500 Index is shown with all dividends reinvested and does not reflect any reduction in performance for the effects of transaction costs or management fees. The S&P 500 Index and the Barclays Bond Index are used for comparative purposes only, and are not meant to be indicative of the Fund's performance, asset composition, or volatility. Because indices cannot be invested in directly, these index returns do not reflect a deduction for fees, expenses, or taxes. The Fund's expense ratio is 1.01%. The expense ratio includes acquired fund fees and expenses which are incurred indirectly by the Fund as a result of investments in securities issued by one or more investment companies.*

Cumulative Return	FAAFX	Barclays Bond Index	S&P 500 Index
1-Year	-6.33%	+5.19%	+15.43%
3-Year	-13.84%	+12.57%	+37.36%
5-Year	+47.48%	+16.39%	+113.44%
Since Inception	+8.40%	+24.12%	+94.91%

Annualized Return	FAAFX	Barclays Bond Index	S&P 500 Index
1-Year	-6.33%	+5.19%	+15.43%
3-Year	-4.84%	+4.03%	+11.16%
5-Year	+8.08%	+3.08%	+16.37%
Since Inception	+1.41%	+3.83%	+12.30%

The Fund's 30-Day SEC Yield at September 30, 2016, was 2.28%.

THE FAIRHOLME ALLOCATION FUND

FAAFX

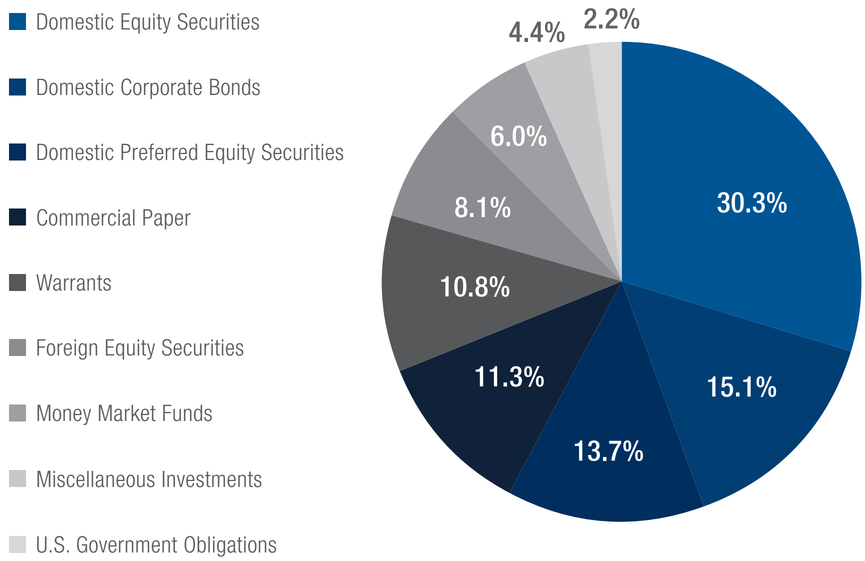
Top Holdings by Issuer as of 8/31/16[4]

Top Holdings by Issuer as of 8/31/16[4]	% FAAFX
Cash and Cash Equivalents	19.5%
Seritage Growth Properties	18.9%
Chesapeake Energy Corp.	11.4%
Sears Holdings Corp.	11.1%
Federal National Mortgage Association	7.2%
Bank of America Corp.	7.0%
Federal Home Loan Mortgage Corp.	6.5%
Imperial Metals Corp.	5.7%
Atwood Oceanics, Inc.	3.7%
American International Group, Inc.	3.0%

Investment Minimums

Initial, Regular Account[5]	$10,000
Initial, IRA[5]	$5,500
Subsequent, Regular Account and IRA	$1,000
Subsequent, Automatic Investment Plan	$250/month

Portfolio Composition by Security Type as of 8/31/16



The Fund seeks long-term total return from capital appreciation and income. The Manager attempts, under normal circumstances, to achieve this investment objective by investing opportunistically in a focused portfolio of investments in the equity, fixed-income and cash and cash-equivalent asset classes. The proportion of the Fund's portfolio invested in each asset class will vary from time to time based on the Manager's assessment of relative fundamental values of securities and other investments in the class, the attractiveness of the investment opportunities within each asset class, general market and economic conditions, and expected future returns of investments. There is no guarantee that the Fund will meet its objective.

(1) This chart assumes that distributions have been reinvested and does not include the effect of taxes.
(2) This figure represents the depreciation 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 Fund.
(4) Percentages were calculated aggregating all securities held of a particular issuer.
(5) The minimum initial investment for regular accounts and IRAs may be waived by the Manager in its discretion.

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Contacts

SHAREHOLDER SERVICES
Fairholme Funds, Inc.
c/o BNY Mellon Investment Servicing (US) Inc.
4400 Computer Drive
Westborough, MA 01581-1722

MANAGER
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4400 Biscayne Boulevard
Miami, FL 33137

INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM
Deloitte & Touche LLP
1700 Market Street
Philadelphia, PA 19103

CUSTODIAN
The Bank of New York Mellon
225 Liberty Street
New York, NY 10286

DISTRIBUTOR
Fairholme Distributors, LLC
899 Cassatt Road
Berwyn, PA 19312

LEGAL
Seward & Kissel, LLP
901 K Street NW
Washington, DC 20001

The Fund's investment objective, risks, charges, and expenses should be considered carefully before investing. The prospectus and summary prospectus contain this and other important information about the Fund, and may be obtained by calling Shareholder Services at (866) 202-2263 or visiting our website www.fairholmefunds.com. Read them carefully before investing.