

Mutual fund investing involves risks, including possible loss of principal. Unless otherwise specified, all information is shown as of January 25, 2019. Past performance information quoted below does not guarantee future results. The investment return and principal value of an investment in The Fairholme Focused Income Fund ("The Income Fund" or the "Fund") will fluctuate so that the value of 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 below. Performance figures reflect the deduction of expenses and assume reinvestment of dividends and capital gains. 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 Fund maintains a focused portfolio of investments in a limited number of issuers and does not seek to diversify its investments. This exposes the Fund to the risk of unanticipated industry conditions and risks particular to a single company or the securities of a single company within its portfolio. Current and future portfolio holdings are subject to change and risk. The Bloomberg Barclays U.S. Aggregate Bond Index (the "Bloomberg Barclays Bond Index") is a broad-based flagship benchmark that measures the investment grade, U.S. dollar denominated, fixed-rate taxable bond market, and includes Treasuries, government-related and corporate securities, mortgage-backed securities (agency fixed rate and hybrid adjustable-rate mortgage pass-throughs), asset-backed securities and commercial mortgage backed securities (agency and non-agency). The Bloomberg Barclays Bond Index is used for comparative purposes only, and is not meant to be indicative of the Fund's performance, asset composition, or volatility. The Fund's performance may differ markedly from the performance of the Bloomberg Barclays Bond Index in either up or down market trends. Because an index cannot be invested in directly, the index returns do not reflect a deduction for fees, expenses, or taxes. The expense ratio for the Fund reflected in the current prospectus dated March 29, 2018, is 1.00%, and may differ from the actual expenses incurred by the Fund for the period covered by the Fund's Annual Report.

Effective January 1, 2018, the Manager agreed to waive, on a voluntary basis, a portion of the management fee of the Fund to the extent necessary to limit the management fee paid to the Manager by the Fund to an annual rate of 0.80% of the Fund's daily average net asset value. This undertaking may be terminated by the Manager upon 60 days' written notice to the Fund.

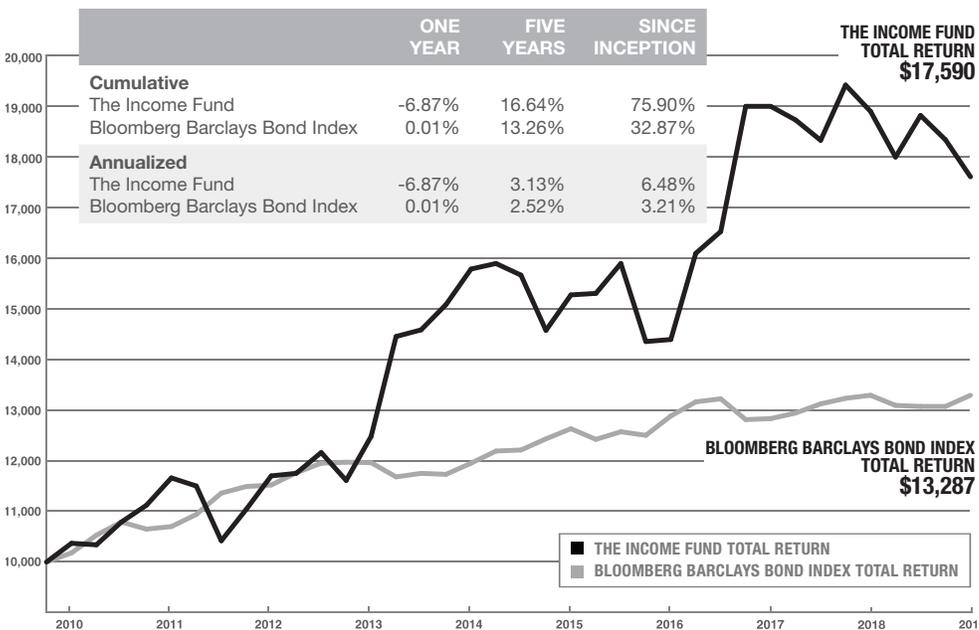
The Portfolio Manager's Report is not part of The Fairholme Funds, Inc. Annual Report due to forward-looking statements that, by their nature, cannot be attested to, as required by regulation. The Portfolio Manager's Report is based on calendar-year performance. A more formal Management Discussion and Analysis is included in the Annual Report. Opinions of the Portfolio Manager are intended as such, and not as statements of fact requiring attestation.

January 25, 2019

To the Shareholders and Directors of The Fairholme Focused Income Fund:

Last year the Fund produced a negative return and trailed its benchmark index, primarily due to the Chapter 11 filing of Sears Holdings and below plan operating performance at Imperial Metals. Performance for the past five years and since inception tells a much more uplifting story, and the new year is off to a good start. The Fund remains focused on long-term outperformance of the Bloomberg Barclays Bond Index by employing a non-diversified strategy to generate current income with the possibility of capital gains.

The Income Fund



TOP ISSUERS (% OF NET ASSETS)	
Cash and Cash Equivalents*	65.7%
Imperial Metals Corp.	9.0%
GMAC Capital Trust I, Inc.	3.7%
The Goldman Sachs Group, Inc.	3.6%
Vista Outdoor, Inc.	3.5%
Citigroup, Inc.	2.8%
Federal Home Loan Mortgage Corp.	2.6%
Chesapeake Energy Corp.	2.3%
Bank of America Corp.	2.2%
Tech Data Corp.	1.3%

The Income Fund's 30-Day SEC Yield at December 31, 2018, was 3.69% (subsidized) and 3.49% (unsubsidized).\*\*

The chart on the left covers the period from inception of The Income Fund (December 31, 2009) through December 31, 2018.

The Income Fund decreased 6.87% versus a 0.01% gain for the Bloomberg Barclays Bond Index in 2018. The above graph and performance table compare The Income Fund's unaudited performance (after expenses) with that of the Bloomberg Barclays Bond Index, with dividends and distributions reinvested, for various periods ending December 31, 2018. The value of a \$10,000 investment in The Income Fund at its inception was worth \$17,590 (assumes reinvestment of distributions into additional Income Fund shares) compared to \$13,287 for the Bloomberg Barclays Bond Index at year-end. Of the \$17,590 the value of reinvested distributions was \$7,760.

\*Includes cash, U.S. Treasury Bills, money market funds, and various commercial paper issuers.

\*\*The 30-Day SEC Yield represents net investment income earned by The Income Fund over the 30-Day period, expressed as an annual percentage rate based on The Income Fund's share price at the end of the 30-Day period. The 30-Day unsubsidized SEC Yield does not reflect any fee waivers/reimbursements/limits in effect.

**Imperial Metals Corporation**

At 9% of Fund assets, the senior unsecured debt of Imperial Metals is the only investment greater than 5% of the Fund. The company is in a robust process to assess strategic alternatives, including the establishment of a joint venture to accelerate development of a world class copper and gold mine in British Columbia. Trading at less than 70 cents on the dollar and maturing in March of this year, this investment alone has the potential in our view to significantly increase the Fund performance in the short-term should a joint venture be established with a credible strategic partner.

**Asset Allocation**

Almost two-thirds of the Fund is invested in investment grade commercial paper with an average maturity of less than two weeks, U.S. Treasury Bills, and money market funds to minimize duration and credit risks. Remaining assets are diversified across high-yield corporate bonds, high-yield preferred stocks, and variable rate bank preferred stocks to improve overall current yield and total return.

**Outlook**

The Federal Reserve increased interest rates by 100 basis points last year. U.S. federal and overall state budget deficits continue to soar in the midst of full employment and economic expansion. Financial markets are more volatile, but not cheap. Year-to-date, the Fund is up 2.34%. The Fund's net assets stand at \$186 million. I and other Fairholme-affiliates own 36.3 % of total Fund shares.

Respectfully submitted,



Bruce R. Berkowitz  
Manager

*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 Fund, and it may be obtained by calling Shareholder Services at (866) 202-2263 or visiting our website [www.fairholmefunds.com](http://www.fairholmefunds.com). Read it carefully before investing.*