

FAIRHOLME

Ignore the crowd.

“(E)ven the intelligent investor is likely to need considerable willpower to keep from following the crowd.”

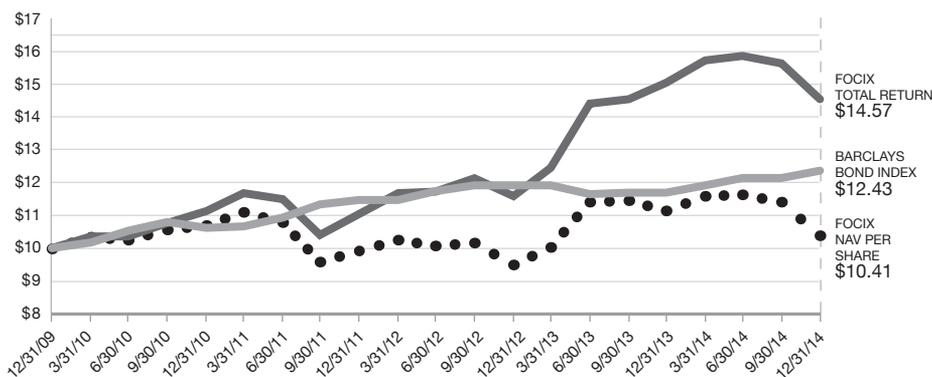
Benjamin Graham

Mutual fund investing involves risks, including loss of principal. The chart below covers the period from inception of The Fairholme Focused Income Fund (December 31, 2009) to December 31, 2014. 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 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 below. Performance figures 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 1.866.202.2263. The Fairholme Focused Income Fund maintains a focused portfolio of investments in a limited number of issuers and does not seek to diversify its investments. This exposes The Fairholme Focused Income Fund to the risk of unanticipated industry conditions and risks particular to a single company or the securities of a single company. The Fairholme Focused Income Fund's performance may differ markedly from the performance of the Barclays Capital U.S. Aggregate Bond Index in either up or down market trends. The Barclays Capital U.S. Aggregate 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. Because indices cannot be invested in directly, these index returns do not reflect a deduction for fees, expenses, or taxes. The Fairholme Focused Income Fund's expense ratio reflected in its prospectus dated March 28, 2014, is 1.01%, which included acquired fund fees and expenses that are incurred indirectly by The Fairholme Focused Income Fund as a result of investments in securities issued by one or more investment companies. Since the close of business on February 28, 2013, the sale of shares of The Fairholme Focused Income Fund has been suspended to new investors, subject to certain exceptions.

January 28, 2015

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

The Fairholme Focused Income Fund (the "Fund" or "FOCIX") decreased 3.39%, versus an increase of 5.97% for the Barclays Capital U.S. Aggregate Bond Index (the "Barclays Bond Index"), in 2014. Since inception, the Fund increased 45.70% versus 24.31% for the Barclays Bond Index. The following table compares the Fund's unaudited performance (after expenses) with that of the Barclays Bond Index, with dividends and distributions reinvested, for the period that ended December 31, 2014.



	ONE YEAR	THREE YEARS	SINCE INCEPTION (12/31/2009)
Cumulative			
FOCIX	(3.39)%	32.02%	45.70%
Barclays Bond Index	5.97%	8.20%	24.31%
Annualized			
FOCIX	(3.39)%	9.70%	7.81%
Barclays Bond Index	5.97%	2.66%	4.45%

The Fund's 30-Day SEC Yield at December 31, 2014, was 4.05%.

- FOCIX Return
- Barclays Bond Index
- FOCIX NAV

At December 31, 2014, the value of a \$10.00 investment in the Fund at its inception was worth \$14.57 (calculated by assuming reinvestment of distributions into additional Fund shares) compared to \$12.43 for the Barclays Bond Index. FOCIX returned 1.9 times more than the Barclays Bond Index on a \$10.00 investment over five years. Of the \$14.57, the share price (net asset value per share) was \$10.41 and the value of distributions reinvested was \$4.16. This difference, more than anything, demonstrates how the Fund has outperformed the market (as represented by the Barclays Bond Index) over the period shown.

The fifth anniversary of the Fund was unceremoniously marked by a weak Q4 2014 performance, largely due to the early October decline in the value of Fannie Mae and Freddie Mac preferred stock following an unfavorable ruling by a federal district court judge. Despite posting a 3.39% decline for 2014, the Fund's performance over the last five years was almost double that of the Barclays Bond Index. The fact that such outperformance was achieved while holding an average of 35% in cash and equivalents since inception validates our barbell strategy for the Fund. Maintaining ample liquidity allows us to take advantage of unexpected opportunities and helps balance a focused portfolio of higher-yielding securities from companies that we understand well. At December 31, 2014, the Fund is composed of securities from eight issuers (71.1%) along with U.S. Treasury Bills and money market funds (28.1%).

Intermediate-term corporate bonds from Sears Holdings due 2018 (30.0%) and Imperial Metals due 2019 (22.1%) both yield roughly 9% to maturity and are attractive coupons to clip because, in our opinion, their actual "issuer default risk" is simply not commensurate with their purported "issuer default rating" (both CCC). The ongoing transformation at Sears accelerated in 2014, with various corporate actions (including the spin-off of Lands' End and Sears Canada) generating over \$2.4 billion in proceeds to the parent. Our analysis of the company's vast asset base (including, but not limited to, its real estate portfolio) provides us with ample confidence that these bonds are covered. While we did not participate in the initial offering by Imperial Metals of attractive 7% senior unsecured notes in March, the Fund was able to take advantage of late summer stress and subsequently buy the notes at a 9% yield to maturity following the unexpected breach at the Mount Polley tailings pond, which caused operations to cease at that site and consequently delayed the eagerly awaited start of the massive Red Chris mine. Investigations to date reveal no injuries, no significant differences in the ecosystem, and no definitive reasons for the accident. We expect that Imperial will overcome this delay of game and resume normal operations.

The preferred stock of Fannie Mae (4.5%) and Freddie Mac (4.9%) do not currently pay dividends due to the terms of the federal conservatorship. Yet, we believe there is potential for significant appreciation in principal over time (and perhaps the recoupment of accrued interest) as the indispensability of these two publicly traded, shareholder-owned companies to affordable homeownership eventually overpowers the taboo imposed upon them by the Washington establishment. Following the substantial price decline at the beginning of the fourth quarter, the Fund purchased more preferred stock – and we continue to believe that these securities have an unusually attractive risk/reward dynamic. On October 10, Fairholme Funds, Inc. (“Fairholme”) filed a notice of appeal in the U.S. Court of Appeals for the District of Columbia of the ruling by District Court Judge Royce Lamberth that dismissed one of Fairholme’s suits against the Federal Housing Finance Agency and U.S. Department of the Treasury. Fairholme’s statement at the time is worth reiterating:

“Fairholme believes strongly that the Net Worth Sweep – imposed four years after the financial crisis – was not authorized by the Housing and Economic Recovery Act of 2008 (“HERA”) and must be unwound. Fairholme also believes strongly that the Federal Housing Finance Agency (“FHFA”) has contractual and fiduciary duties to the preferred shareholders of Fannie Mae and Freddie Mac, and that these duties can and will be enforced.”

“The resolution provisions of HERA are virtually identical to those that apply to U.S. banks. We are confident that Congress did not authorize the conservator – a Federal agency – to operate a profitable financial institution perpetually, to strip away all of its capital, to pay all its future profits to another Federal agency, to violate the order of priorities of corporate law, to transfer its assets without determining fair price, to replace the organized claims process of receivership with the self-dealing expropriation of private property, or to make corporate governance decisions without a standard of care. And yet, if the D.C. District Court’s opinion stands, FHFA is authorized to do all of this with impunity, previously and forever. In fact, the District Court opined that it lacks the authority even to review the conservator’s actions – a fundamentally flawed interpretation of the statute. After all, why would Congress write a 260-page HERA statute specifying and limiting the conservator’s powers if no court has jurisdiction to enforce it? Where there is no remedy, there is no law.”

More recently, the November 19 statement by Senate Banking Chairman Tim Johnson at a congressional hearing revealed uncommon pragmatism on Capitol Hill, as he noted: “There is only so much that can be accomplished while [Fannie Mae and Freddie Mac] are in limbo. Everyone agrees that the conservatorship cannot continue forever, so I hope my colleagues will keep working toward a more certain future for the market. However, if Congress cannot agree on a smooth, more certain path forward, I urge you [FHFA Director] Watt to engage the Treasury Department in talks to end the conservatorship.” Progress in Washington requires patience, but we continue to believe that common sense will ultimately prevail and lead to a viable solution that benefits all stakeholders.

Preferred stocks of Ally Financial (4.4%), Chesapeake Energy (2.7%), Goldman Sachs (1.4%), and Bank of America (1.2%) have current yields exceeding 5% and, on the whole, we believe are well positioned to perform favorably in a rising interest rate environment.

The Fund’s significant cash position will be opportunistically deployed as we look to take advantage of select market dislocations in 2015.

Respectfully submitted,



Bruce R. Berkowitz
Managing Member
Fairholme Capital Management

The Portfolio Manager’s Report is not part of The Fairholme Focused Income Fund’s 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 and precedes a more formal Management Discussion and Analysis. Opinions of the Portfolio Manager are intended as such, and not as statements of fact requiring attestation.

FAIRHOLME

Ignore the crowd.

The Fairholme Focused Income Fund (FOCIX)
Seeking current income

Annual Report 2014

Managed by Fairholme Capital Management

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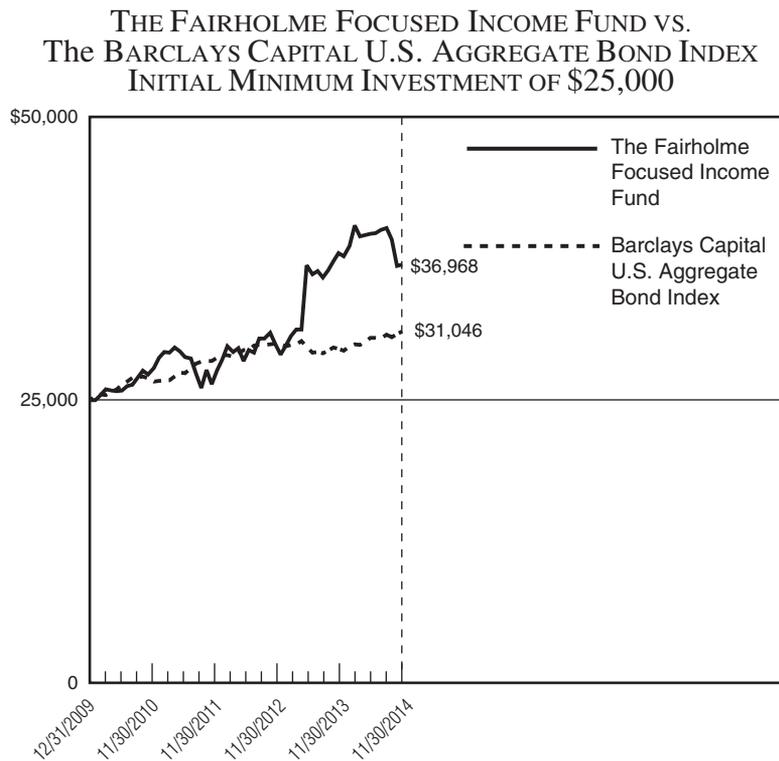
THE FAIRHOLME FOCUSED INCOME FUND

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THE FAIRHOLME FOCUSED INCOME FUND

FUND PERFORMANCE (unaudited)
Inception through November 30, 2014



The Fairholme Focused Income Fund (the “Fund”) commenced operations on December 31, 2009. The chart above presents the performance of a \$25,000 investment from inception to the latest fiscal year ending November 30, 2014.

The following notes pertain to the chart above as well as to the performance table included in the Management Discussion & Analysis Report. **Performance information in this report represents past performance and is not a guarantee of 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 quoted within. The performance information does not reflect the taxes an investor would pay on Fund distributions or upon redemption of Fund shares. 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.**

Data for both the Barclays Capital U.S. Aggregate Bond Index and the Fund are presented assuming all dividends and distributions have been reinvested and do not reflect any taxes that might have been incurred by a shareholder as a result of the Fund distributions. The Barclays Capital U.S. Aggregate Bond Index is an unmanaged market weighted index comprised of investment grade corporate bonds (rated BBB or better), mortgages, and U.S. Treasury and government agency issues with at least one year to maturity and does not reflect any investment management fees or transaction expenses, nor the effects of taxes, fees, or other charges.

THE FAIRHOLME FOCUSED INCOME FUND

MANAGEMENT DISCUSSION & ANALYSIS For the Fiscal Year Ended November 30, 2014

The Fairholme Focused Income Fund (the “Fund”) shares outstanding and audited net asset value per share (“NAV”) at November 30, 2014, the end of the Fund’s fiscal year, and per share NAVs at other pertinent dates, were as follows:

<u>11/30/2014 Shares Outstanding</u>	<u>11/30/2014 NAV (audited)</u>	<u>05/31/2014 NAV (unaudited)</u>	<u>11/30/2013 NAV (audited)</u>
19,971,990	\$10.82	\$11.72	\$11.98

At December 31, 2014, the unaudited per share NAV of the Fund was \$10.41. Performance figures below are shown for the Fund’s fiscal year ended November 30, 2014, and do not match calendar year figures for the period ended December 31, 2014, cited in the Portfolio Manager’s report.

<u>Fund Performance to 11/30/2014</u>	<u>Six Months</u>	<u>One Year</u>	<u>Since Inception 12/31/2009</u>
Cumulative:			
Fund	(6.83)%	(2.67)%	47.87%
Barclays Bond Index	1.91%	5.26%	24.18%
Annualized:			
Fund		(2.67)%	8.28%
Barclays Bond Index		5.26%	4.50%

For the six months ended November 30, 2014, the Fund was outperformed by the Barclays Capital U.S. Aggregate Bond Index (“Barclays Bond Index”) by 8.74 percentage points while over the last year the Fund was outperformed by the Barclays Bond Index by 7.93 percentage points. From inception, the Fund outperformed the Barclays Bond Index by 3.78 percentage points per annum, or on a cumulative basis, 23.69 percentage points over four years and eleven months, respectively.

Fairholme Capital Management, L.L.C. (the “Manager”) believes performance over shorter periods is likely to be less meaningful than performance over longer periods. Investors are cautioned not to rely on short-term results. The fact that securities increase or decline in value does not always indicate that the Manager believes these securities to be more or less attractive — in fact, the Manager believes that some price increases present selling opportunities and some price declines present buying opportunities.

Further, shareholders should note that the Barclays Bond Index is an unmanaged index incurring no fees, expenses, or tax effects and is shown solely to compare Fund performance to that of an unmanaged and diversified index.

Shareholders are also cautioned that it is possible that some securities mentioned in this discussion may no longer be held by the Fund subsequent to the end of the fiscal period and that the Fund may have made significant new purchases that are not yet required to be disclosed. It is the Fund’s general policy not to disclose portfolio holdings other than when required by relevant law or regulation. Portfolio holdings are subject to change without notice.

Not all Fund portfolio dispositions or additions are material, and, while the Fund and the Manager have long-term objectives, it is possible that a security sold or purchased in one period will be purchased or sold in a subsequent period. Generally, the Manager determines to buy and sell based on its estimates of the absolute and relative intrinsic values and fundamental dynamics of a particular security and its issuer and its industry. However, certain strategies of the Manager in carrying out Fund policies may result in shorter holding periods.

The Manager invests Fund assets in securities to the extent it finds reasonable investment opportunities in accordance with its Prospectus and may invest a significant portion of Fund assets in liquid, low-risk securities or cash. The Manager views liquidity as a strategic advantage. At November 30, 2014, cash and cash equivalents (consisting of cash, commercial paper, deposit accounts, U.S. Treasury Bills, and money-market funds) represented 33.78% of total assets. Since inception, the Fund has held liquid, low-risk securities or cash for periods without negatively influencing performance, although there is no guarantee that future performance will not be negatively affected by Fund liquidity.

THE FAIRHOLME FOCUSED INCOME FUND

MANAGEMENT DISCUSSION & ANALYSIS (continued) For the Fiscal Year Ended November 30, 2014

The Fund is considered to be “non-diversified” under the Investment Company Act of 1940. The Fund can invest a greater percentage of assets in fewer securities than a diversified fund and may invest a significant portion of cash and liquid assets in one or more higher-risk securities at any time, particularly in situations where markets are weak or a particular security declines sharply. The Fund may also have a greater percentage of assets invested in a particular industry than a diversified fund, exposing the Fund to the risk of an unanticipated industry condition as well as risks specific to a single company or security. For the fiscal year ended November 30, 2014, the Fund investments that performed the best were Sears Holdings Corp. and JC Penney Corp., Inc. The biggest contributors to negative performance were investments in Federal National Mortgage Association and Federal Home Loan Mortgage Corp. The following charts show the top holdings by issuer and sector in descending order of net assets as of November 30, 2014.

The Fairholme Focused Income Fund Top Holdings by Issuer* (% of Net Assets)		The Fairholme Focused Income Fund Top Sectors (% of Net Assets)	
Sears Holdings Corp.	29.1%	Cash and Cash Equivalents**	33.8%
Imperial Metals Corp.	20.4%	Retail Department Stores	29.1%
Ally Financial, Inc.	4.3%	Metals & Mining	20.4%
Federal National Mortgage Association	3.7%	Mortgage Finance	5.4%
Chesapeake Energy Corp.	2.8%	Consumer Finance	4.3%
Bank of America Corp.	2.2%	Oil & Natural Gas Exploration	2.8%
Federal Home Loan Mortgage Corp.	1.7%	Diversified Banks	2.2%
The Goldman Sachs Group, Inc.	1.3%	Capital Markets	1.3%
	<u>65.5%</u>		<u>99.3%</u>

* Excludes cash, U.S. Treasury Bills, and money market funds.

** Includes cash, U.S. Treasury Bills, and money market funds.

The Manager views the ability to focus on fewer investments than a diversified fund as a strategic advantage. However, such a strategy may negatively influence short-term performance and there is no guarantee that long-term performance will not be negatively affected.

The Fund may invest in non-U.S. securities and securities of corporations domiciled outside of the United States, which may expose the Fund to adverse changes resulting from foreign currency fluctuations or other potential risks as described in the Fund’s Prospectus and Statement of Additional Information.

The Fund’s officers, the Board of Directors (the “Board” or the “Directors”), and the Manager are aware that large cash inflows or outflows may adversely affect Fund performance. Such flows are monitored and appropriate actions are contemplated for when such flows could negatively impact performance.

Since inception, the Fund has been advised by the Manager. Bruce Berkowitz, both the Managing Member of the Manager and Chairman of the Fund’s Board, continues to have a significant personal stake in the Fund, holding an aggregate 537,918 shares at November 30, 2014. While there is no requirement that Mr. Berkowitz own shares of the Fund, such holdings are believed to help align the interests of the Manager with the interests of the shareholders.

The Board, including the Independent Directors, continues to believe that it is in the best interests of the Fund to have Mr. Berkowitz serve as Chairman of the Board given: his long-term relative performance; his experience, commitment, and significant personal investment in the Fund; the present constitution of Directors and policies; and current rules and regulations. A Director and Officers of the Fund are also Officers of the Manager. Nevertheless, at November 30, 2014, a majority of Directors were independent of the Manager, no stock option or restricted stock plans exist, Officers received no direct compensation from the Fund, and the Director affiliated with the Manager received no compensation for being a Director.

For more complete information about the Fund, or to obtain a current Prospectus, please visit www.fairholmefunds.com or call Shareholder Services at 1-866-202-2263.

THE FAIRHOLME FOCUSED INCOME FUND

EXPENSE EXAMPLE

For the Six Month Period from June 1, 2014
through November 30, 2014 (unaudited)

As a Fund shareholder, you incur direct and indirect costs. Direct costs include, but are not limited to, transaction fees at some broker-dealers, custodial fees for retirement accounts and wire transfer fees. You also incur indirect, ongoing costs that include, but are not limited to, management fees paid to the Manager.

The following example is intended to help you understand your indirect costs (also referred to as “ongoing costs” and measured in dollars) when investing in the Fund and to compare these costs with the ongoing costs of investing in other mutual funds. This example is based on an investment of \$1,000 invested in the Fund at June 1, 2014, and held for the entire six month period ending November 30, 2014.

Actual Expenses

The first line of the table below provides information about actual account values and actual expenses. You may use the information in this line, together with the amount you had invested at the beginning of the period, to estimate the expenses that you paid over the period. Simply divide your account value by \$1,000 (for example, an \$8,600 account value divided by \$1,000 = 8.6), then multiply the result by the number in the first line under the heading “Expenses Paid During the Period” to estimate the expenses you paid on your Fund holdings during this period.

Hypothetical Example for Comparison Purposes

The second line of the table provides information about hypothetical account values and hypothetical expenses based on the Fund’s actual expense ratio and an assumed rate of return of 5% per year before expenses, which is not the Fund’s actual return for the period presented. The hypothetical account values and expenses may not be used to estimate the actual ending account balance or expenses that you paid for the period presented. However, you may use this information to compare ongoing costs of investing in the Fund with the ongoing costs of investing in other funds. To do so, compare this 5% hypothetical example with the 5% examples that appear in the shareholder reports of other funds.

Please note that the column titled “Expenses Paid During the Period” in the table below is meant to highlight your ongoing costs only and do not reflect any transactional costs, such as redemption fees (if any), or other direct costs. Therefore, the second line of the table is useful in comparing ongoing costs only, and will not help you determine the relative total costs of owning different funds. In addition, if these direct costs were included, your total costs would be higher.

Fund	Beginning Account Value June 1, 2014	Ending Account Value November 30, 2014	Annualized Expense Ratio	Expenses Paid During the Period June 1, 2014 Through November 30, 2014*
Actual	\$1,000.00	\$ 931.70	1.00%	\$4.84
Hypothetical (5% return before expenses)	\$1,000.00	\$1,020.05	1.00%	\$5.06

* Expenses are equal to the Fund’s annualized expense ratio, multiplied by the average account value over the period, multiplied by 183 days/365 days (to reflect the one-half year period).

THE FAIRHOLME FOCUSED INCOME FUND

SCHEDULE OF INVESTMENTS
November 30, 2014

Shares		Value	Principal		Value
	DOMESTIC PREFERRED EQUITY SECURITIES — 16.0%			DOMESTIC CORPORATE BONDS — 29.1%	
	CAPITAL MARKETS — 1.3%			RETAIL DEPARTMENT STORES — 29.1%	
143,000	The Goldman Sachs Group, Inc., Preferred, 4.000%, Series D	\$ 2,834,260	\$67,574,000	Sears Holdings Corp. 6.625%, 10/15/2018	\$ 62,776,246
2,600	The Goldman Sachs Group, Inc., Preferred, 4.000%, Series C	51,870			
		2,886,130		TOTAL DOMESTIC CORPORATE BONDS (COST \$65,417,360)	<u>62,776,246</u>
	CONSUMER FINANCE — 4.3%			FOREIGN CORPORATE BONDS — 20.4%	
9,200	Ally Financial, Inc., Preferred, 7.000%, Series G ^(a)	9,222,908		CANADA — 20.4%	
				METALS & MINING — 20.4%	
190,000	Bank of America Corp., Preferred, 4.000%, Series 5	3,868,400	47,200,000	Imperial Metals Corp. 7.000%, 03/15/2019 ^(a)	44,160,320
40,000	Bank of America Corp., Preferred, 4.000%, Series 4	840,000			
		4,708,400		TOTAL FOREIGN CORPORATE BONDS (COST \$43,758,809)	<u>44,160,320</u>
	MORTGAGE FINANCE — 5.4%			U.S. GOVERNMENT OBLIGATIONS — 25.4%	
1,029,724	Federal Home Loan Mortgage Corp., Preferred, 6.550%, Series Y ^(b)	3,655,520	10,000,000	U.S. Treasury Bills 0.051%, 12/04/2014 ^(d)	9,999,958
1,167,500	Federal National Mortgage Association, Preferred, 7.000%, Series O ^{(b)(c)}	7,635,450	10,000,000	U.S. Treasury Bills 0.051%, 01/22/2015 ^(d)	9,999,271
100,000	Federal National Mortgage Association, Preferred, 7.750%, Series S ^{(b)(c)}	432,000	35,000,000	U.S. Treasury Bills 0.107%, 04/30/2015 ^(d)	34,991,985
		11,722,970		TOTAL U.S. GOVERNMENT OBLIGATIONS (COST \$54,987,489)	<u>54,991,214</u>
	OIL & NATURAL GAS EXPLORATION — 2.8%		<u>Shares</u>	MONEY MARKET FUNDS — 8.4%	
60,300	Chesapeake Energy Corp., Preferred, 5.000%	5,969,700	18,202,531	Fidelity Institutional Money Market Funds - Money Market Portfolio, 0.090% ^(e)	18,202,531
				TOTAL MONEY MARKET FUNDS (COST \$18,202,531)	<u>18,202,531</u>
	TOTAL DOMESTIC PREFERRED EQUITY SECURITIES (COST \$37,924,012)	<u>34,510,108</u>			

The accompanying notes are an integral part of the financial statements.

THE FAIRHOLME FOCUSED INCOME FUND

SCHEDULE OF INVESTMENTS (continued)
November 30, 2014

	<u>Value</u>
TOTAL INVESTMENTS — 99.3%	
(COST \$220,290,201)	\$ 214,640,419
OTHER ASSETS IN	
EXCESS OF	
LIABILITIES — 0.7%	<u>1,406,242</u>
NET ASSETS — 100.0%	<u>\$ 216,046,661</u>

^(a) Restricted security as defined in Rule 144A under the Securities Act of 1933. The Manager has determined that such security is liquid pursuant to the Fund's liquidity guidelines. The value of these securities totals \$53,383,228, which represents 24.71% of the Fund's net assets.

^(b) Non-income producing security.

^(c) Variable rate security. Rate shown is the effective rate as of November 30, 2014.

^(d) Rates shown are the effective yields based on the purchase price. The calculation assumes the security is held to maturity.

^(e) Annualized based on the 1-day yield as of November 30, 2014.

The accompanying notes are an integral part of the financial statements.

THE FAIRHOLME FOCUSED INCOME FUND

STATEMENT OF ASSETS & LIABILITIES
November 30, 2014

Assets

Investments, at Fair Value (Cost — \$220,290,201)	\$214,640,419
Interest Receivable	1,281,102
Receivable for Investments Sold	615,836
Receivable for Capital Shares Sold	156,000
Total Assets	<u>216,693,357</u>

Liabilities

Payable for Investments Purchased	444,000
Accrued Management Fees	178,042
Payable for Capital Shares Redeemed	24,654
Total Liabilities	<u>646,696</u>

NET ASSETS

\$216,046,661

Net Assets Consist of:

Paid-In Capital	\$217,452,703
Accumulated Undistributed Net Investment Income	1,421,920
Accumulated Net Realized Gain on Investments and Foreign Currency Related Transactions	2,821,820
Net Unrealized Depreciation on Investments and Foreign Currency Related Translations	<u>(5,649,782)</u>

NET ASSETS

\$216,046,661

Shares of Common Stock Outstanding* (\$0.0001 par value)	<u>19,971,990</u>
Net Asset Value, Offering and Redemption Price Per Share (\$216,046,661 / 19,971,990 shares)	<u>\$ 10.82</u>

* 200,000,000 shares authorized in total.

The accompanying notes are an integral part of the financial statements.

THE FAIRHOLME FOCUSED INCOME FUND

STATEMENT OF OPERATIONS

	For the Fiscal Year Ended November 30, 2014
Investment Income	
Interest	\$ 5,878,936
Dividends (net of \$1,420 in foreign taxes withheld)	<u>1,099,392</u>
Total Investment Income	<u>6,978,328</u>
Expenses	
Management Fees	<u>2,374,534</u>
Total Expenses	<u>2,374,534</u>
Net Investment Income	<u>4,603,794</u>
Realized and Unrealized Gain (Loss) on Investments and Foreign Currency Related Transactions	
Net Realized Gain on Investments and Foreign Currency Related Transactions	2,795,505
Net Change in Unrealized Appreciation (Depreciation) on Investments and Foreign Currency Related Translations	<u>(13,798,701)</u>
Net Realized and Unrealized Loss on Investments and Foreign Currency Related Translations	<u>(11,003,196)</u>
NET DECREASE IN NET ASSETS FROM OPERATIONS	<u><u>\$ (6,399,402)</u></u>

The accompanying notes are an integral part of the financial statements.

THE FAIRHOLME FOCUSED INCOME FUND

STATEMENTS OF CHANGES IN NET ASSETS

	<u>For the Fiscal Year Ended November 30, 2014</u>	<u>For the Fiscal Year Ended November 30, 2013</u>
CHANGES IN NET ASSETS		
From Operations		
Net Investment Income	\$ 4,603,794	\$ 10,576,270
Net Realized Gain on Investments	2,795,505	23,074,399
Net Change in Unrealized Appreciation (Depreciation) on Investments and Foreign Currency Related Translations	<u>(13,798,701)</u>	<u>25,139,412</u>
Net Increase (Decrease) in Net Assets from Operations	<u>(6,399,402)</u>	<u>58,790,081</u>
From Dividends and Distributions to Shareholders		
Net Investment Income	(3,837,576)	(14,560,171)
Net Realized Capital Gains from Investment Transactions	<u>(13,876,149)</u>	<u>—</u>
Net Decrease in Net Assets from Dividends and Distributions	<u>(17,713,725)</u>	<u>(14,560,171)</u>
From Capital Share Transactions		
Proceeds from Sale of Shares	30,025,869	28,234,083
Shares Issued in Reinvestment of Dividends and Distributions	14,885,867	12,435,924
Cost of Shares Redeemed	<u>(51,739,852)</u>	<u>(95,341,938)</u>
Net Decrease in Net Assets from Shareholder Activity	<u>(6,828,116)</u>	<u>(54,671,931)</u>
NET ASSETS		
Net Decrease in Net Assets	(30,941,243)	(10,442,021)
Net Assets at Beginning of Year	<u>246,987,904</u>	<u>257,429,925</u>
Net Assets at End of Year	<u>\$216,046,661</u>	<u>\$246,987,904</u>
Accumulated Undistributed Net Investment Income at End of Year	<u>\$ 1,421,920</u>	<u>\$ 682,102</u>
SHARES TRANSACTIONS		
Issued	2,609,016	2,718,394
Reinvested	1,322,790	1,214,865
Redeemed	<u>(4,568,532)</u>	<u>(9,017,977)</u>
Net Decrease in Shares	(636,726)	(5,084,718)
Shares Outstanding at Beginning of Year	<u>20,608,716</u>	<u>25,693,434</u>
Shares Outstanding at End of Year	<u>19,971,990</u>	<u>20,608,716</u>

The accompanying notes are an integral part of the financial statements.

THE FAIRHOLME FOCUSED INCOME FUND

FINANCIAL HIGHLIGHTS

	For the Fiscal Year Ended November 30, 2014	For the Fiscal Year Ended November 30, 2013	For the Fiscal Year Ended November 30, 2012	For the Fiscal Year Ended November 30, 2011	For the Period Ended November 30, 2010 ⁽¹⁾
PER SHARE OPERATING PERFORMANCE					
NET ASSET VALUE, BEGINNING OF PERIOD	\$11.98	\$10.02	\$9.71	\$10.70	\$10.00
Investment Operations					
Net Investment Income ⁽²⁾	0.22	0.46	0.97	0.64	0.45
Net Realized and Unrealized Gain (Loss) on Investments	(0.51)	2.12	0.31	(0.95)	0.45
Total from Investment Operations	(0.29)	2.58	1.28	(0.31)	0.90
Dividends and Distributions					
From Net Investment Income	(0.19)	(0.62)	(0.97)	(0.64)	(0.20)
From Realized Capital Gains	(0.68)	—	—	(0.04)	—
Total Dividends and Distributions	(0.87)	(0.62)	(0.97)	(0.68)	(0.20)
NET ASSET VALUE, END OF PERIOD	\$10.82	\$11.98	\$10.02	\$9.71	\$10.70
TOTAL RETURN	(2.67)%	26.91%	13.45%	(3.24)%	9.05% ⁽³⁾
Ratio/Supplemental Data					
Net Assets, End of Period (in 000's)	\$216,047	\$246,988	\$257,430	\$299,224	\$364,235
Ratio of Expenses to Average Net Assets:					
Before Expenses Waived	1.00%	1.00%	1.00%	1.00%	1.00% ⁽⁴⁾
After Expenses Waived	1.00% ⁽⁵⁾	1.00% ⁽⁵⁾	0.91% ⁽⁵⁾	0.67%	0.50% ⁽⁴⁾
Ratio of Net Investment Income to Average Net Assets	1.94%	4.28%	9.53%	5.96%	4.69% ⁽⁴⁾
Portfolio Turnover Rate	38.86%	42.87%	8.27%	91.67%	77.03% ⁽³⁾

⁽¹⁾ The Fund commenced operations on December 31, 2009.

⁽²⁾ Based on average shares outstanding.

⁽³⁾ Not Annualized.

⁽⁴⁾ Annualized.

⁽⁵⁾ Effective March 29, 2012, the Manager's contractual management fee waiver/expense reimbursement for the Fund expired.

The accompanying notes are an integral part of the financial statements.

Note 1. Organization

Fairholme Funds, Inc. (the “Company”), a Maryland corporation, is registered under the Investment Company Act of 1940, as amended (the “1940 Act”), as an open-end management investment company. The Company’s Articles of Incorporation permit the Board of Directors of the Company (the “Board” or the “Directors”) to issue 1,100,000,000 shares of common stock at \$.0001 par value. 200,000,000 shares have been allocated to The Fairholme Focused Income Fund (the “Fund”). The Fund is a non-diversified fund. The Fund may have a greater percentage of its assets invested in particular securities than a diversified fund, exposing the Fund to the risk of unanticipated industry conditions as well as risks specific to a single company or the securities of a single company. The Board has the power to designate one or more separate and distinct series and/or classes of shares of common stock and to classify or reclassify any unissued shares with respect to such series.

The Fund’s investment objective is to seek current income. Under normal circumstances, the Fund seeks to achieve its investment 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 debt securities of issuers in the U.S. and foreign countries, bank debt (including bank loans and loan participations), government and agency debt securities of the U.S. and foreign countries, convertible bonds and other convertible securities and equity securities, including preferred and common stock and interests in real estate investment trusts (“REITs”). Although the Fund normally holds a focused portfolio of securities, the Fund is not required to be fully invested in such securities and may maintain a significant portion of its total assets in cash and securities generally considered to be cash equivalents. Fairholme Capital Management, L.L.C. (the “Manager”) serves as investment adviser to the Fund.

There is no guarantee that the Fund will meet its objectives.

Since the close of business on February 28, 2013, (the “Closing Date”), the sale of shares of the Fund has been suspended to new investors, subject to certain exceptions as described below. Subject to the right of the Fund to reject any order to purchase shares or to withdraw the offering of shares at any time, shares remain available for purchase to existing Fund shareholders. The following categories of new investors may continue to purchase shares of the Fund: (i) clients of financial advisors and financial consultants that have clients invested in the Fund as of the Closing Date; (ii) clients of financial advisors and intermediaries that have approved the inclusion of the Fund as an investment option in their asset allocation programs or discretionary investment programs, including wrap, model or other managed account programs, as of the Closing Date; and (iii) participants in group retirement plans that include the Fund as an investment option as of the Closing Date, and IRA transfers and rollovers from such plans. In addition, Directors of the Company, clients and employees of the Manager and their respective immediate family members may open new accounts and add shares of the Fund to such accounts. The Fund retains the right to limit the foregoing exceptions, make additional exceptions to the suspension of the sale of the Fund’s shares to new investors, and subsequently commence selling its shares to new investors.

Note 2. Significant Accounting Policies

The Fund’s investments are reported at fair value as defined by Accounting Principles Generally Accepted in the United States of America (“U.S. GAAP”). The Fund calculates its net asset value as soon as practicable following the close of regular trading on the New York Stock Exchange (currently 4:00 p.m. Eastern Time) on each day the New York Stock Exchange is open.

A description of the valuation techniques applied to the Fund’s securities measured at fair value on a recurring basis follows:

Security Valuation:

Equity securities (common and preferred stocks): Securities traded on a national securities exchange or reported on the NASDAQ national market are generally valued at the official closing price, or at the last reported sale price on the exchange or market on which the securities are traded, as of the close of business on the day the securities are being valued or, lacking any sales, at the last available bid price. To the extent these securities are actively traded and valuation adjustments are not applied, they are classified in Level 1 of the fair value hierarchy. If these securities are not actively traded, they are classified

THE FAIRHOLME FOCUSED INCOME FUND

NOTES TO FINANCIAL STATEMENTS (continued)
November 30, 2014

in Level 2. The Manager may also employ other valuation methods which the Manager believes would provide a more accurate indication of fair value. In these situations, if the inputs are observable, the valuation will be classified in Level 2 of the fair value hierarchy, otherwise they would be classified in Level 3.

Fixed-income securities (U.S. government obligations, corporate bonds, convertible bonds, and asset backed securities): The fair value of fixed-income securities is estimated using market quotations when readily available, but may also be estimated by various methods when no such market quotations exist and when the Manager believes these other methods reflect the fair value of such securities. These methods may consider recently executed transactions in securities of the issuer or comparable issuers and market price valuations from independent pricing services and/or brokers (where observable). Where the Manager deems it appropriate to do so (such as when independent prices are unavailable or not deemed to be representative of fair value) fixed-income securities will be fair valued in good faith following consideration by, and conclusion of, the Manager's Valuation Committee. As of November 30, 2014, long-term fixed-income securities are valued by the Manager utilizing the average bid of independent broker/dealer quotes and/or the average of valuations from independent pricing services. Although fixed-income securities are classified in Level 2 of the fair value hierarchy at November 30, 2014, in instances where lower relative weight is placed on transaction prices, quotations, or similar observable inputs, they would be classified in Level 3.

Open-end mutual funds: Investments in open-end mutual funds including money market funds are valued at their closing net asset value each business day and are classified in Level 1 of the fair value hierarchy.

Short-term securities: Investments in securities with maturities of less than sixty days when acquired or long-term securities, which are within sixty days of maturity are estimated by using the amortized cost method of valuation, which the Manager and the Board have determined will approximate fair value. To the extent the inputs are observable and timely, the values would be classified in Level 2 of the fair value hierarchy.

Restricted securities: Depending on the relative significance of valuation inputs, these instruments may be classified in any level of the fair value hierarchy.

Warrants: The Fund may invest in warrants, which may be acquired either through a direct purchase, included as part of a private placement, or pursuant to corporate actions. Warrants entitle, but do not obligate, the holder to buy equity securities at a specific price for a specific period of time. Warrants may be considered more speculative than certain other types of investments in that they do not entitle a holder to dividends or voting rights with respect to the underlying securities that may be purchased nor do they represent any rights in the assets of the issuing company. Also, the value of a warrant does not necessarily change with the value of the underlying securities and a warrant ceases to have value if it is not exercised prior to its expiration date. Warrants traded on a security exchange are valued at the official closing price on the valuation date and are classified as Level 1 of the fair value hierarchy. Over the counter (OTC) warrants are valued using simulation models utilizing market value of the underlying security, expiration date of the warrants, volatility of the underlying security, strike price of the warrants, risk-free interest rate at the valuation date, and are classified as Level 2 or Level 3 of the fair value hierarchy depending on the observability of the inputs used.

The Fund uses several recognized industry third-party pricing services (TPPS) - approved by the Board and unaffiliated with the Manager - to value some of its securities. It also uses other independent market trade data sources (such as TRACE, the FINRA-developed mandatory reporting of over-the-counter secondary market transactions), as well as broker quotes provided by market makers. The data within these feeds is ultimately sourced from major stock exchanges and trading systems where these securities trade. If a price obtained from the pricing source is deemed unreliable, it may be discarded and/or challenged. In these cases the pricing decision is made by reference to the reliable market data from the other market data sources.

The Manager may determine the fair valuation of a security when market quotations are insufficient or not readily available, when securities are determined to be illiquid or restricted, or when in the judgment of the Manager the prices or values available do not represent the fair value of the instrument. Factors which may cause the Manager to make such a judgment include the following: (a) only a bid price or an asked price is available; (b) the spread between bid and asked prices is

THE FAIRHOLME FOCUSED INCOME FUND

NOTES TO FINANCIAL STATEMENTS (continued)
November 30, 2014

substantial; (c) the liquidity of the securities; (d) the frequency of sales; (e) the thinness of the market; (f) the size of reported trades; (g) actions of the securities markets, such as the suspension or limitation of trading; and (h) bona fide bids or offers made to the Manager by independent third parties. Among the factors to be considered to fair value a security are recent prices of comparable securities that are publicly traded, reliable prices of securities not publicly traded, the use of valuation models, current analyst reports, valuing the income or cash flow of the issuer, or cost if the preceding factors do not apply. The circumstances of Level 3 securities are frequently monitored to determine if fair valuation measures continue to apply.

The Manager reports quarterly to the Board the results of the application of fair valuation policies and procedures.

The inputs and valuation techniques used to measure fair value of the Fund's investments are summarized into three levels as described in the hierarchy below:

- Level 1 — quoted prices in active markets for identical securities;
- Level 2 — other significant observable inputs (including quoted prices for similar securities, quoted prices in inactive markets for identical securities, interest rates, prepayment speeds, credit risk, etc.); and
- Level 3 — significant unobservable inputs (including the Manager's determination as to the fair value of investments).

The inputs or methodology used for valuing investments are not necessarily an indication of the level of risk associated with investing in those investments. The summary of the Fund's investments by inputs used to value the Fund's investments as of November 30, 2014, is as follows:

	Valuation Inputs		Total Fair Value at 11/30/2014
	Level 1 – Quoted Prices	Level 2 – Other Significant Observable Inputs	
ASSETS:			
INVESTMENTS (Fair Value):			
Domestic Preferred Equity Securities			
Consumer Finance	—	\$ 9,222,908	\$ 9,222,908
Other*	\$25,287,200	—	25,287,200
Domestic Corporate Bonds*	—	62,776,246	62,776,246
Foreign Corporate Bonds*	—	44,160,320	44,160,320
U.S. Government Obligations	—	54,991,214	54,991,214
Money Market Funds	18,202,531	—	18,202,531
TOTAL INVESTMENTS	<u>\$43,489,731</u>	<u>\$171,150,688</u>	<u>\$214,640,419</u>

* Industry classifications for these categories are detailed in the Schedule of Investments.

The Fund had no transfers between Level 1 and Level 2 during the fiscal year ended November 30, 2014. The Fund's policy is to recognize transfers among Levels as of the beginning of the reporting period.

There were no Level 3 investments at November 30, 2014, or November 30, 2013.

Recent Accounting Standards: In June 2013, the Financial Accounting Standards Board (the "FASB") issued guidance that creates a two-tiered approach to assess whether an entity is an investment company. The guidance will also require an investment company to measure noncontrolling ownership interest in other investment companies at fair value and will require additional disclosures relating to investment company status, any changes thereto and information about financial support provided or contractually required to be provided to any of the investment company's investees. The guidance is effective for financial statements with fiscal years beginning on or after December 15, 2013, and interim periods within those fiscal years. Management is evaluating the impact of this guidance on the Fund's financial statement disclosures.

THE FAIRHOLME FOCUSED INCOME FUND

NOTES TO FINANCIAL STATEMENTS (continued)
November 30, 2014

Dividends and Distributions: The Fund records dividends and distributions to shareholders on the ex-dividend date. The Fund intends to declare and pay net investment income distributions, if any, quarterly in March, June, September, and December. The Fund intends to distribute any net long-term capital gains and any net short-term capital gains at least once a year. If the total dividends and distributions made in any tax year exceeds net investment income and accumulated realized capital gains, a portion of the total distribution may be treated as a tax return of capital.

Foreign Currency Translation: The books and records of the Fund are maintained in U.S. dollars. Foreign currency amounts are translated into U.S. dollars on the following basis: (i) fair value of investment securities, assets, and liabilities at the current rate of exchange; and (ii) purchases and sales of investment securities, income, and expenses at the relevant rates of exchange prevailing on the respective dates of such transactions. The Fund does not isolate that portion of gains and losses on investment securities which is due to changes in the foreign exchange rates from that which is due to changes in the market prices of such securities.

Estimates: The preparation of financial statements in conformity with U.S. GAAP requires the Fund to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of both contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reported period. Actual results could differ from those estimates.

Other: The Fund accounts for security transactions on the trade date for financial statement purposes. The specific identification method is used for determining gains or losses for financial statements and income tax purposes. Dividend income is recorded on the ex-dividend date net of foreign taxes withheld where recovery is uncertain and interest income is recorded on an accrual basis. Discounts and premiums on securities purchased are amortized over the life of the respective securities using the effective yield method. Securities denominated in currencies other than U.S. dollars are subject to changes in value due to fluctuation in exchange rates. The Fund may invest in countries that require governmental approval for the repatriation of investment income, capital, or the proceeds of sales of securities by foreign investors. In addition, if there is deterioration in a country's balance of payments or for other reasons, a country may impose temporary restrictions on foreign capital remittances abroad.

The Fund paid commissions and other brokerage fees during the period.

Note 3. Related Party Transactions

The Manager is a Delaware limited liability company and is registered with the Securities and Exchange Commission as an investment adviser. The Manager's principal business and occupation is to provide investment management and advisory services to individuals, corporations, and other institutions throughout the world. Pursuant to an Investment Management Agreement, the Fund pays a management fee to the Manager for its provision of investment advisory and operating services to the Fund. Subject to applicable waivers or limitations, the management fee is paid at an annual rate equal to 1.00% of the daily average net assets of the Fund. Under the Investment Management Agreement, the Manager is responsible for paying all of the Fund's expenses, including expenses for the following services: transfer agency, fund accounting, fund administration, custody, legal, audit, compliance, directors' fees, call center, fulfillment, travel, insurance, rent, printing, postage, and other office supplies, and excluding commissions, brokerage fees, and other transaction costs, taxes, interest, litigation expenses, and related expenses, and other extraordinary expenses.

Effective March 29, 2012, the Manager's contractual management fee waiver/expense reimbursement for the Fund expired. Prior to March 29, 2012, the Manager had contractually agreed to waive a portion of its management fee and/or limit the Fund's operating expenses (excluding taxes, interest, brokerage commissions, acquired fund fees and expenses, expenses incurred in connections with any merger or reorganization and extraordinary expenses such as litigation) so that the Fund's operating expenses, after such waiver or limitation payment, would not exceed an annual rate of 0.75% of the Fund's daily average net assets for the period March 30, 2011 to March 29, 2012. For the period December 31, 2009 to March 30, 2011, the Manager had contractually agreed to waive a portion of its management fee and/or limit the Fund's operating expenses

THE FAIRHOLME FOCUSED INCOME FUND

NOTES TO FINANCIAL STATEMENTS (continued)
November 30, 2014

(excluding those expenses noted above) so that the Fund's operating expenses, after such waiver or limitation payment, would not exceed an annual rate of 0.50% of the Fund's daily average net assets. The Manager may be reimbursed for fee waivers and/or expense limitation payments made in any fiscal year of the Fund over the following three fiscal years. Any reimbursement is subject to the Board's review and approval. A reimbursement may be requested by the Manager if the aggregate amount paid by the Fund for operating expenses for such fiscal year, taking into account any reimbursement, does not exceed the fee waiver/expense limitation in place at the time of the initial waiver or reimbursement of the amount by the Manager. For the fiscal year ended November 30, 2014, the Manager may request reimbursement of up to the following:

For the period ended November 30, 2012, expiring November 30, 2015:	\$249,582
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The Manager earned \$2,374,534 from the Fund for its services during the fiscal year ended November 30, 2014.

Affiliates of the Manager held in aggregate 537,918 shares at November 30, 2014.

A Director and Officers of the Fund are also the Managing Member and Officers of the Manager or its affiliates.

Note 4. Investments

For the fiscal year ended November 30, 2014, aggregated purchases and sales of investment securities other than short-term investments and U.S. government obligations were as follows:

<u>Purchases</u>	<u>Sales</u>
\$106,053,633	\$47,648,962

Note 5. Tax Matters

Federal Income Taxes: The Fund intends to qualify each year as a "Regulated Investment Company" under Subchapter M of the Internal Revenue Code of 1986, as amended. By so qualifying, the Fund will not be subject to federal income taxes to the extent that it distributes all of its net investment income and any realized capital gains.

For U.S. federal income tax purposes, the cost of securities owned, gross unrealized appreciation, gross unrealized depreciation, and net unrealized appreciation of investments at November 30, 2014, were as follows:

<u>Cost</u>	<u>Gross Unrealized Appreciation</u>	<u>Gross Unrealized Depreciation</u>	<u>Net Unrealized Depreciation</u>
\$220,407,948	\$600,202	\$(6,367,731)	\$(5,767,529)

The difference between book basis and tax basis net unrealized appreciation is attributable to capitalized cost.

The Fund's tax basis capital gains are determined at the end of each fiscal year. Therefore, the components of distributable earnings on a tax basis were as follows:

Undistributed Ordinary Income*	\$ 1,421,920
Net Long-Term Capital Gain	2,939,567
Net Unrealized Appreciation on Investments and Foreign Currency Related Transactions	<u>(5,767,529)</u>
Total	<u><u>\$(1,406,042)</u></u>

* Inclusive of short-term capital gain

The Fund had no net capital loss carryforwards available to reduce future required distributions of net capital gains to shareholders.

Under the Regulated Investment Company Modernization Act of 2010, capital losses originating in taxable years beginning after December 22, 2010 ("post-enactment capital losses") are carried forward indefinitely. In addition, these losses must be

THE FAIRHOLME FOCUSED INCOME FUND

NOTES TO FINANCIAL STATEMENTS (continued)
November 30, 2014

utilized prior to the losses incurred in pre-enactment taxable years. Furthermore, post-enactment capital losses will retain their character as either short-term or long-term capital losses rather than being considered all short-term capital losses as under previous law.

The Manager has analyzed the Fund's tax positions taken on tax returns for all open tax years (current and prior three tax years) and has concluded that there are no uncertain tax positions that require recognition of a tax liability. The Fund's federal and state income and federal excise tax returns for tax years for which the applicable statutes of limitations have not expired (the current year and prior three years) are subject to examination by the Internal Revenue Service and state departments of revenue. Additionally, the Fund is not aware of any tax position for which it is reasonably possible that the total amounts of unrecognized tax benefits will change materially in the next twelve months.

Note 6. Dividends and Distributions to Shareholders

Ordinary income and capital gain distributions are determined in accordance with federal income tax regulations, which may differ from U.S. GAAP.

The tax character of dividends and distributions paid by the Fund were as follows:

	<u>For the Fiscal Year Ended November 30, 2014</u>	<u>For the Fiscal Year Ended November 30, 2013</u>
Dividends and Distributions paid from:		
Ordinary Income	\$ 3,837,576	\$14,560,171
Long-Term Capital Gain	<u>13,876,149</u>	<u>—</u>
	<u>\$17,713,725</u>	<u>\$14,560,171</u>

The Fund declared and made payable the following distribution on December 29, 2014:

Dividends and Distributions paid from:	
Ordinary Income	\$2,028,542
Long-Term Capital Gain	<u>2,939,655</u>
	<u>\$4,968,197</u>

Note 7. Reclassification in the Capital Accounts

In accordance with U.S. GAAP, the Fund has recorded reclassifications in their capital accounts. These reclassifications have no impact on the net asset value of the Fund and are designed generally to present undistributed income and realized gains on a tax basis which is considered to be more informative to the shareholder. Permanent differences are primarily due to the tax treatment of distributions from partnerships to the Fund. As of November 30, 2014, the Fund recorded the following reclassifications to increase (decrease) the accounts listed below:

Accumulated Undistributed Net Investment Income	\$(26,400)
Accumulated Net Realized Gain	26,400

Note 8. Indemnifications

Under the Company's organizational documents, its Officers and Directors are indemnified against certain liabilities arising out of the performance of their duties to the Fund. In the normal course of business the Company or the Fund enter into contracts that contain a variety of representations and customary indemnifications. The Fund's maximum exposure under these arrangements is unknown as this would involve future claims that may be made against the Fund that have not yet occurred. However, based on its experience to date, the Fund expects the risk of loss to be remote.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors of Fairholme Funds, Inc. and
the shareholders of The Fairholme Focused Income Fund:

We have audited the accompanying statement of assets and liabilities, including the schedule of investments, of The Fairholme Focused Income Fund (the "Fund"), as of November 30, 2014, and the related statement of operations for the year then ended, the statements of changes in net assets for each of the two years in the period then ended, and the financial highlights for each of the periods presented. These financial statements and financial highlights are the responsibility of the Fund's management. Our responsibility is to express an opinion on these financial statements and financial highlights based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements and financial highlights are free of material misstatement. The Fund is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Fund's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. Our procedures included confirmation of securities owned as of November 30, 2014, by correspondence with the custodian and brokers. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements and financial highlights referred to above present fairly, in all material respects, the financial position of The Fairholme Focused Income Fund as of November 30, 2014, the results of its operations for the year then ended, the changes in its net assets for each of the two years in the period then ended, and the financial highlights for each of the periods presented, in conformity with accounting principles generally accepted in the United States of America.

DELOITTE & TOUCHE LLP

Philadelphia, Pennsylvania
January 29, 2015

THE FAIRHOLME FOCUSED INCOME FUND

ADDITIONAL INFORMATION
November 30, 2014

Board of Directors (unaudited)

The Board of Directors has overall responsibility for conduct of the Company's affairs. The day-to-day operations of the Fund are managed by the Manager, subject to the By-Laws of the Company and review by the Company's Board. The Directors and Officers of the Company, including those Directors who are also officers, are listed below.

Name, Age & Address†	Position(s) Held, Term of Office & Length of Time Served**	Principal Occupation(s) During Past 5 Years§	Number of Portfolios in Fund Complex Overseen by Director	Other Current Directorships Held by Director
Interested Directors and Officers				
Bruce R. Berkowitz* Age 56	Mr. Berkowitz has served as a Director & President of the Company since December 15, 1999.	Managing Member, Fairholme Capital Management, LLC since October 1997.	3	Director and Chairman of the Board of Directors, The St. Joe Co.
Cesar L. Alvarez, Esq.* Age 67	Mr. Alvarez has served as a Director of the Company since May 19, 2008.	Co-Chairman of Greenberg Traurig, LLP since 2013; Executive Chairman of Greenberg Traurig, LLP from 2010 to 2013; Chief Executive Officer of Greenberg Traurig, LLP from October 1997 to 2010.	3	Chairman, Board of Directors, Mednax, Inc.; Director, Intrexon Corp., Sears Holdings Corp., The St. Joe Co., and Watsco, Inc.
Independent Directors^				
Terry L. Baxter Age 69	Mr. Baxter has served as a Director of the Company since May 19, 2008.	Chairman of the Board, CEO, Source One (retired); President of White Mountain Holdings (retired).	3	Director, Main Street America Group
Howard S. Frank Age 73	Mr. Frank has served as a Director of the Company since May 7, 2007.	Chairman of the Board of Costa Crociere S.p.A. since 2014; Special Advisor to the CEO and to the Chairman of Carnival Corporation & plc. since 2013; Vice Chairman, Chief Operating Officer and Director, Carnival Corporation & plc. from 1989 to 2013.	3	Director, New World Symphony; Director, The St. Joe Co.
Steven J. Gilbert Age 67	Mr. Gilbert has served as a Director of the Company since June 16, 2014	Chairman, Gilbert Global Equity Partners, L.P. since 1998; Vice Chairman, MidOcean Equity Partners, L.P. since 2005; Co-Chairman, Birch Grove Capital since 2013; Senior Managing Director and Chairman, Sun Group (USA) from 2007 to 2009.	3	Chairman, CPM Holdings, Inc.; Director, MBIA, Inc.; Lead Independent Director, Empire State Realty Trust; Lead Independent Director, TRI Pointe Homes, Inc.; Director, Waterpik, Inc., Freshpet, Inc. and Plia Systems, Inc.
Avivith Oppenheim, Esq. Age 64	Ms. Oppenheim has served as a Director of the Company since December 15, 1999.	Attorney-at-Law.	3	None.
Leigh Walters, Esq. Age 68	Mr. Walters has served as a Director of the Company since December 15, 1999.	Vice-President and Director, Valcor Engineering Corporation. Attorney-at-Law.	3	Director, Valcor Engineering Corporation

† Unless otherwise indicated, the address of each Director of the Company is c/o Fairholme Capital Management, LLC, 4400 Biscayne Blvd., 9th Floor, Miami, FL 33137.

^ Directors who are not "interested persons" of the Company as defined under the 1940 Act.

* Mr. Berkowitz and Mr. Alvarez are each an interested person, as defined in the 1940 Act, of the Company because of their affiliation with the Manager.

** Each Director serves for an indefinite term. Each officer serves for an annual term and until his or her successor is elected and qualified.

§ The information reported includes the principal occupation during the last five years for each Director and other information relating to the professional experiences, attributes and skills relevant to each Director's qualifications to serve as Director.

THE FAIRHOLME FOCUSED INCOME FUND

ADDITIONAL INFORMATION (continued)
November 30, 2014

Officers (unaudited)

Name, Age & Address†	Position(s) Held with the Company	Term of Office & Length of Time Served*	Principal Occupation(s) During Past 5 Years
Fred Fraenkel Age 65	Vice President	Mr. Fraenkel has served as Vice President of the Company since January 2013.	President of Fairholme Capital Management, L.L.C. since January 2013; Chief Research Officer, Fairholme Capital Management, L.L.C. since October 2011; Vice Chairman Beacon Trust Company from 2008 to 2011.
Wayne Kellner Age 45	Treasurer	Mr. Kellner has served as Treasurer of the Company since March 2012.	Chief Operating Officer, Fairholme Capital Management, L.C.C. since June 2014; Chief Financial Officer, Fairholme Capital Management, L.L.C. since January 2012; Treasurer, Fairholme Capital Management, L.L.C. from January 2011 to December 2011; Tax Principal, Rothstein Kass from 2006 to 2010.
Paul R. Thomson Age 58	Chief Compliance Officer and Secretary	Mr. Thomson has served as Chief Compliance Officer of the Company since April 2010 and has served as Secretary since June 2011. Mr. Thomson previously served as Chief Compliance Officer from November 2008 to January 2009.	Chief Compliance Officer, Fairholme Capital Management LLC since April 2010; Chief Financial Officer, Fairholme Capital Management LLC from January 2008 to January 2012.

† Unless otherwise indicated, the address of each Officer of the Company is c/o Fairholme Capital Management, LLC, 4400 Biscayne Blvd., 9th Floor, Miami, FL 33137.

* Each officer serves for an annual term and until his or her successor is elected and qualified.

Approval of Investment Management Agreement (unaudited)

At its meeting on October 21, 2014, the Board of Directors (the “Board” or the “Directors”) of Fairholme Funds, Inc. (the “Company”) approved the renewal of the investment management agreement between the Company, on behalf of The Fairholme Focused Income Fund (the “Fund”), and Fairholme Capital Management, L.L.C. (the “Manager”). In considering whether to approve the renewal of the agreement, the Directors considered the factors discussed below, and information made available to them at the meeting relating to such factors, and other information they deemed relevant. The renewal of the agreement was not, however, based on any single factor, but on an evaluation of the totality of factors and information reviewed and evaluated by the Directors.

A. Nature, Extent and Quality of Services

The Directors considered information provided to them concerning the services performed by the Manager for the Fund pursuant to the agreement. The Directors reviewed information concerning the nature, extent and quality of investment advisory and operational services provided, or overseen, by the Manager. The Directors reviewed information concerning the personnel responsible for the day-to-day portfolio and administrative management of the Fund, the overall reputation of the Manager and the Manager’s current and planned staffing levels. The Directors considered the Manager’s commitment to the Fund as evidenced, among other things, by the current share ownership of the Fund by management/owners/employees of the Manager. The Directors considered information describing the Manager’s compliance policies and procedures, including recent updates to those policies and information concerning the policies designed to address the Fund’s compliance with its investment objective, policies and restrictions and applicable regulatory requirements and to address the Manager’s conflicts of interest in providing services to the Fund and to other advisory clients.

The Directors did not compare services provided by the Manager to the Fund with the services provided by Manager to its other advisory accounts because such accounts are not subject to the same regulatory requirements as the Fund, may have different investment restrictions, holdings and goals than the Fund and require different levels of client and back-office servicing than the Fund.

The Directors concluded that the nature, extent and quality of services provided by the Manager to the Fund was appropriate and sufficient to support renewal of the agreement.

B. Investment Performance

The Directors considered information regarding the Fund’s performance, the Manager’s views on performance and the holdings of the Fund that contributed negatively and positively to the Fund’s performance. The Directors considered information about the investment performance of the Fund, including information reflecting that the Fund had outperformed its relevant index, the Barclays Capital US Aggregate Bond Index, by approximately 6.5 percentage points for the twelve months ended August 31, 2014, and by nearly 38 percentage points cumulatively since inception to August 31, 2014. The Directors also reviewed and considered a comparison, prepared by a third-party (Lipper), of the Fund’s performance and the performance of similarly situated mutual funds for the 1-year, 3-year and since inception periods to August 31, 2014, which reflected that, in those periods, the Fund’s performance exceeded the average and median performance of the peer group.

C. Management Fee and Expense Ratio

The Directors considered information about the Fund’s management fee and expense ratio, including information in the third party report comparing the Fund’s management fee and the most recent expense ratio to the advisory fees and expense ratios of other similarly situated mutual funds. The Directors noted that, unlike many of the peer group funds, the Fund’s management fee covers many of the Fund’s operating and other expenses. The Directors also noted that, for the Fund, the total expense ratio for its latest full fiscal year was lower than the median expense ratio of the most recently completed fiscal year of its peer group funds included in the third party report.

In evaluating the management fee and expense ratio information, the Directors took into account the demands and complexity of portfolio management for the Fund in light of its investment objective, strategies, and asset size. The Directors also considered information regarding the Manager's payment (in some cases from its resources) of certain expenses for the benefit of the Fund, including shareholder account-level expenses associated with certain omnibus accounts. The Directors also reviewed information concerning the fees paid to the Manager by its other advisory accounts.

After reviewing information presented to them concerning fees, expenses, performance and other matters, the Directors concluded that the Fund's management fee and overall expense ratio were reasonable in light of the services provided by or through the Manager.

D. Profitability

The Directors considered information regarding the estimated profitability of the Fund to the Manager. They considered such profitability in light of the Fund's assets under management, overall expense ratio, performance and the services provided by or through the Manager, and concluded that the Manager's estimated profitability was not such as to prevent Directors from approving the renewal of the agreement.

E. Economies of Scale

The considered information concerning economies of scale for the Fund, including the current assets of the Fund. The Directors concluded for the Fund that no modification to the Fund's existing arrangements was warranted based on economies of scale.

Proxy Voting Policies, Procedures and Records (unaudited)

The Company has adopted policies and procedures that provide guidance and set forth parameters for the voting of proxies relating to securities held in the Fund's portfolio. A description of these policies and procedures, and records of how the Fund voted proxies relating to their portfolio securities during the most recent twelve month period ended June 30, 2014, are available to you upon request and free of charge by writing to the Fairholme Funds, Inc., c/o BNY Mellon Investment Servicing (US) Inc., P.O. Box 9692, Providence, RI, 02940 or by calling Shareholder Services at 1-866-202-2263 or by visiting our website at www.fairholmefunds.com. They may also be obtained by visiting the Securities and Exchange Commission ("SEC") website at www.sec.gov. The Company shall respond to all shareholder requests for records within three business days of its receipt of such request by first-class mail or other means designed to ensure prompt delivery.

N-Q Filing (unaudited)

The Company files a complete schedule of the Fund's portfolio holdings on Form N-Q for the fiscal quarters ending February 28 (February 29 during leap year) and August 31. The Form N-Q filing must be made within 60 days of the end of the quarter. The Forms N-Q relating to the Fund's portfolio investments are available on the SEC's website at www.sec.gov, or may be reviewed and copied at the SEC's Public Reference Room in Washington, DC (call 1-800-732-0330 for information on the operation of the Public Reference Room).

THE FAIRHOLME FOCUSED INCOME FUND

ADDITIONAL INFORMATION (continued)
November 30, 2014

Shareholder Tax Information (unaudited)

The Fund reported \$17,713,725 of total distributions paid during the fiscal year ended November 30, 2014, and \$13,876,149 of that represented long-term capital gain distributions.

The information below is reported for the Fund's fiscal year and not calendar year. Therefore, shareholders should refer to their Form 1099-DIV or other tax information which will be mailed in 2015 to determine the calendar year amounts to be included on their 2014 tax returns. Shareholders should consult their own tax advisors.

Please note that, for the fiscal year ended November 30, 2014, the respective percentages of ordinary income distributions paid by the Fund were reported as follows:

<u>Distribution Period November 30, 2014</u>	<u>The Fund</u>
Qualified Dividend Income for Individuals	18.02%
Dividends Qualifying for the Dividends Received Deduction for Corporations	19.07%
Qualifying Interest Income	87.29%
U.S. Treasury Securities	1.48%*

* The law varies in each state as to whether and what percentage of dividend income attributable to U.S. Treasury securities is exempt from state and local income tax. It is recommended that you consult your tax advisor to determine if any portion of the dividends you received is exempt from income taxes.

All information reported is based on financial information available as of the date of this annual report and, accordingly, are subject to change. For each item, it is the intention of the Fund to report the maximum amount permitted under the Internal Revenue Code and the regulations thereunder.

FAIRHOLME FUNDS

Officers of Fairholme Funds, Inc.

Bruce R. Berkowitz

President

Fred Fraenkel

Vice President

Wayne Kellner

Treasurer

Paul R. Thomson

Chief Compliance Officer & Secretary

Board of Directors of Fairholme Funds, Inc.

Cesar L. Alvarez, Esq.

Terry L. Baxter

Bruce R. Berkowitz

Howard S. Frank

Steven J. Gilbert

Avivith Oppenheim, Esq.

Leigh Walters, Esq.

Investment Manager

Fairholme Capital Management, L.L.C.

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Miami, FL 33137

Transfer Agent, Fund Accountant and Administrator

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King of Prussia, PA 19406

Custodian

The Bank of New York Mellon

1 Wall Street

New York, NY 10286

Independent Registered Public Accounting Firm

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Philadelphia, PA 19103

Legal Counsel

Seward & Kissel LLP

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Washington, DC 20001

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