FAIRHOLME FUNDS
Reprint Disclaimer

THIS DISCLAIMER ACCOMPANIES REPRINTS AND IS PRECEDED BY RELEVANT FAIRHOLME FUNDS FACT SHEETS. THE FUNDS' OBJECIVES, RISKS, CHARGES, AND EXPENSES SHOULD BE CONSIDERED CAREFULLY BEFORE INVESTING. THE FUNDS' PROSPECTUS CONTAINS THIS AND OTHER IMPORTANT INFORMAITON ABOUT THE FUNDS. READ IT CAREFULLY BEFORE INVESTING.

Investing involves risks including loss of principal. Performance information quoted represents past performance and does not guarantee future results. The investment return and principal value of an investment will fluctuate so that an investor's shares may be worth more or less than their original cost. Current performance may be higher or lower than the performance quoted in accompanied materials. The fund imposes a 2% redemption fee on Fairholme Fund and Fairholme Allocation shares held less than 60 days. Performance data does not reflect redemption fees, which would reduce total returns. Current performance may be obtained by calling Shareholder Services at 866-202-2263. Fairholme performance numbers include all expenses, including acquired fund fees and expenses incurred indirectly by the Funds in securities issued by investment companies. While the funds have no front or back loads, or 12b-1 fees, management fees and other expenses still apply.

The Funds are non-diversified, which means that the Funds invest in a smaller number of securities when compared to more diversified funds. The Funds are exposed to greater individual security volatility than diversified funds. The Funds also invest in foreign securities which may involve greater volatility; political, economic, and currency risks; and differences in accounting methods. The Fund may also invest in "special situations" to achieve its objectives. These strategies may involve greater risks than other fund strategies. Investments in debt securities typically decrease in value when interest rates rise. This risk is usually greater for longer-term debt securities. Lower-rated and non-rated securities present greater loss to principal than higher-rated securities. Fund holdings and/or 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.

Funds may hold both equities and/or fixed income securities of specific issuers. Cited top holdings exclude cash and cash equivalents, which include commercial paper, U.S. Treasury Bills, money market funds and deposit accounts. The S&P 500 Index is an unmanaged market index and should not be considered indicative of any Fairholme Funds investment. It is not possible to directly invest in an index. Unlike a mutual fund, the performance of an index assumes no taxes, transaction costs, management fees or other expenses.

Interviews may cite morningstar rating and awards. The Overall Morningstar Rating for a fund is derived from a weighted average of the performance figures associated with its three-, five- and ten-year (if applicable) Morningstar Rating metrics. Each Morningstar average represents a universe of funds with similar investment objectives. References to other mutual funds does not constitute an offer of these securities. Established in 1988, the Morningstar Fund Manager of the Year award recognizes portfolio managers who demonstrate excellent investment skill and the courage to differ from the consensus to benefit investors. To qualify for the award, managers' funds must have not only posted impressive returns for the year, but the managers also must have a record of delivering outstanding long-term performance and of aligning their interests with shareholders'. The Fund Manager of the Year award winners are chosen based on Morningstar's proprietary research and in-depth evaluation by its fund analysts. The 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.

Certain terms may be used in reprints. "Price to earnings ratio" is a common tool for comparing the prices of different common stocks and is calculated by dividing the current market price of a stock by the earnings per share. "Book value" is the net asset value of a company, calculated by subtracting total liabilities from total assets. The adviser defines "free cash flow" as the cash a company would generate annually from operations after all cash outlays necessary to maintain the business in its current condition. "Dividend yield" is the yield a company pays out to its shareholder in the form of dividends.

Opinions expressed are those of the author and/or Fairholme Capital Management, L.L.C. and should not be considered a forecast of future events, a guarantee of future results, nor investment advice.

SHARES OF THE FUNDS ARE DISTRIBUTED BY FAIRHOLME DISTRIBUTORS, INC.

FAIRHOLME

The Fairholme Fund

INVESTMENT OBJECTIVE

The Fairholme Fund seeks long-term growth of its shareholders' capital by investing in equity securities of public companies and by holding a focused portfolio. The Fund's preferred investment strategy is to silently partner with exceptional owner-managers who have demonstrated success, honesty, and integrity. The Fund buys when it finds such companies generating or holding significant cash when compared to market values. Purchases are made without regard to categorization. The Fund also intends to invest in special situations, including, but not limited to, Chapter 11 reorganizations.

Investing in the Fairholme Fund involves risk including loss of principal. The Fairholme Fund is non-diversified, which means that it 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 may also invest in "special situations" to achieve its objectives. These strategies may involve greater risks than other fund strategies. The Fairholme 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. The Fairholme Fund's investments are subject to credit risk. An issuer's credit quality depends on its ability to pay interest on and repay its debt and other obligations. Additionally, investments in fixed-income securities that are rated below investment grade by one or more nationally recognized statistical rating organization or that are unrated and are deemed to be of similar quality ("high yield securities") may be subject to greater risk of loss of principal and interest than investments in higher-rated fixed-income securities.

Please visit *www.fairholmefunds.com* for a prospectus, past reports and advisor letters, and further details on the Fund's philosophy and strategies.

OVERALL MORNINGSTAR RATING as of 12/31/2011

★★★

Among 1,127 Large Value Funds as of 12/31/11.
Based on Risk-Adjusted Returns.

LIPPER RANKING AND % BEATEN as of 12/31/2011

	1 YR	5 YR	10 YR
Rank	301	70	19
% Beaten	0%	67%	82%

As of 12/31/11 the number of funds within the Multi-Cap Value Funds tracked by Lipper was 301, 214, and 108 on a 1-, 5-, and 10-year basis, respectively. Lipper, Inc. is a nationally recognized organization that ranks the performance of mutual funds based on total return which includes reinvested dividends and capital gains, if any, and excludes sales charges. Each fund is ranked within a universe of funds with a similar investment objective.

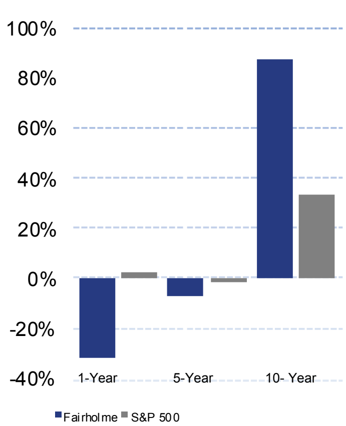
FUND PERFORMANCE as of 12/31/11

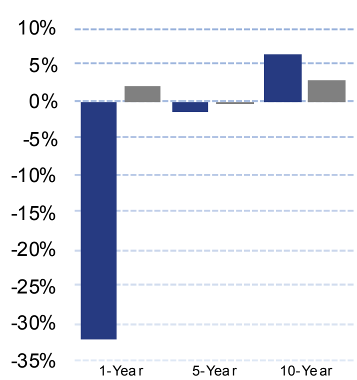
Cumulative Returns

1-Year	-32.42%
5-Year	-6.89%
10-Year	88.40%
Since Inception	199.31%

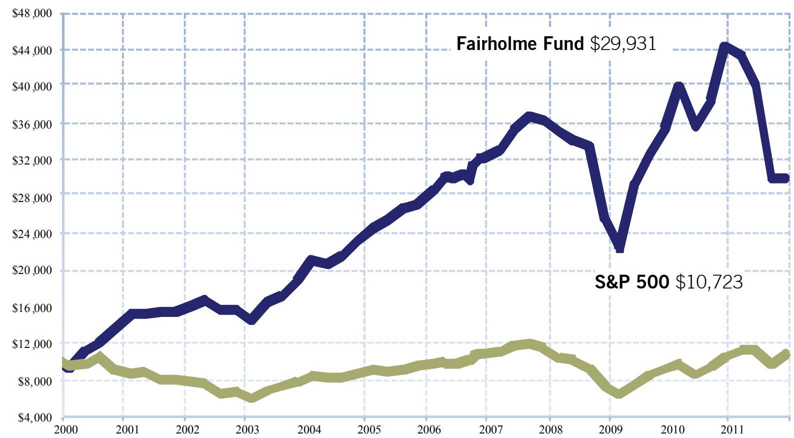
Average Annual Total Returns

1-Year	-32.42%
5-Year	-1.42%
10-Year	6.54%
Since Inception	9.56%
Expense Ratio	1.01%*





GROWTH OF $10,000 from 12/29/99 to 12/31/11

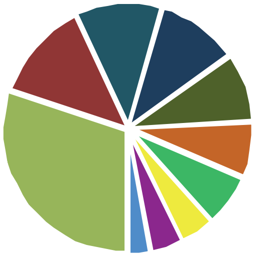


Performance Details

The chart above covers the period from inception of The Fund (December 29, 1999) to December 31, 2011. 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 higher or lower than the performance information quoted above. Performance figures assume reinvestment of dividends and capital gains, but does not reflect the effect of a 2% redemption fee, which is imposed on shares held less than 60 days. If it did, total returns would be reduced. Any questions you may have, including most recent month-end performance, can be answered by calling Shareholder Services at 1-866-202-2263.

The S&P 500 Index is a broad based measurement of changes in the stock market, is used for comparative purposes only, and is not meant to be indicative of the Fund's performance, asset composition or volatility. Given the wide scope of securities held by S&P 500, it should be inherently less volatile. Our results may differ markedly from those of the S&P 500 in either up or down market trends. The performance of the S&P 500 is shown with all dividends reinvested into the index and does not reflect any reduction in performance for the effects of transaction costs or management fees. Investors cannot invest directly in an index.

TOP CATEGORIES



	% of Total Portfolio as of 11/30/11
Multi-Line Insurance	30.0%
Diversified Holding Companies	12.9%
Life Insurance	11.4%
Retail Department Stores	10.7%
Cash and Cash Equivalents**	8.9%
Diversified Banks	7.3%
Commercial Finance	6.9%
Real Estate Management & Development	4.5%
Real Estate Investment Trusts	4.2%
Surety Insurance	2.9%

TOP HOLDINGS BY ISSUER***

as of 11/30/2011

	%of Total Net Assets
American International Group, Inc.	26.2%
AIA Group Ltd.	11.4%
Sears Holdings Corp.	10.7%
Berkshire Hathaway, Inc.	9.3%
CIT Group Inc.	6.9%
Bank of America Corp.	5.5%
General Growth Properties, Inc.	4.2%
The St. Joe Co.	4.0%
China Pacific Insurance (Group) Co., Ltd.	3.8%
Leucadia National Corp.	3.6%
Total	85.6%

STATISTICS

YTD Return (12/31/11)	-32.42%
NAV (12/30/11)	$23.15
12 Month Low-High	$22.87—$36.53
Net Assets ($Millions as of 12/30/11)	$6,962
30-Day SEC Yield	-0.75%
Fiscal Year End	November
Fund Inception	12/29/1999
CUSIP	304871106
Fund Symbol	FAIRX

FEATURES

Minimum Initial Investment	$10,000
Minimum Retirement****	$10,000
Minimum Subsequent Investment	$1,000
Minimum Subsequent Retirement	$1,000
Minimum Automatic Investment Plan	$250

* Includes acquired fund fees of .01%. Acquired fund fees and expenses are those expenses incurred indirectly by the Fund as a result of investments in securities issued by one or more investment companies.

**Cash and Cash Equivalents include investable cash and money market funds.

***Excludes cash and money market funds.

****The minimum initial investment may be waived by the Manager in its discretion.

The fund's investment objectives, risks, charges, and expenses should be considered carefully before investing. The prospectus contains this and other important information about the Fairholme Fund, and it may be obtained by calling shareholder services at 1-866-202-2263 or visiting our website www.fairholmefunds.com. Read it carefully before investing.

Shares of the Fairholme 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.

Fairholme Distributors, Inc. (1/12)

TRANSFER AGENT

The Fairholme Fund
4400 Computer Drive
Westborough, MA 01581-1722
Telephone: 1-866-202-2263
www.fairholmefunds.com

FUND ADVISOR

Fairholme Capital Management, LLC
4400 Biscayne Boulevard
Miami, FL 33137

FAIRHOLME

Ignore the crowd.

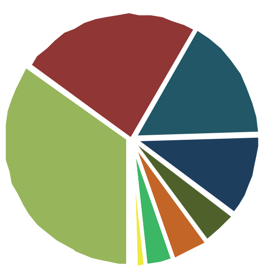
The Fairholme Focused Income Fund

INVESTMENT OBJECTIVE

The Fairholme Focused Income Fund seeks current income, other forms of cash distributions and capital preservation. The Fund attempts 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, but are not limited to, corporate debt securities of issuers in the U.S. and foreign countries, government and agency debt securities of U.S. and foreign countries, bank loans and loan participations, convertible bonds and other convertible securities, and equity securities, including preferred and common stock. The Fund will use Fairholme's focused, multi-sector, multi-strategy, value-based approach. There is no guarantee that the fund will meet its objectives.

Investing in the Fund involves risk including loss of principal. The Fairholme Focused Income Fund is a non-diversified mutual fund, which means that the Fund invests in a smaller number of securities when compared to more diversified funds. This strategy exposes the Fund and its shareholders to greater risk of loss from adverse developments affecting portfolio companies. The 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 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.

TOP CATEGORIES



% of Total Portfolio as of 11/30/11

Surety Insurance	34.0%
Regional Banks	23.0%
Retail Department Stores	15.6%
Commercial Finance	10.4%
Diversified Banks	4.7%
Cash and Cash Equivalents*	4.5%
Capital Markets	3.4%
Real Estate Investment Trusts	1.2%
Multi-Line Insurance	0.5%
Real Estate Management & Development	0.1%

TOP HOLDINGS BY ISSUER**

as of 11/30/11

	%of Total Net Assets
MBIA, Inc.	34.0%
Emigrant Bancorp, Inc.	17.7%
Sears Holdings Corp.	15.6%
CIT Group Inc.	10.4%
Regions Financial Corp.	5.3%
Bank of America Corp.	4.2%
Jeffries Group, Inc.	3.4%
General Growth Properties, Inc.	1.2%
Wells Fargo & Co.	0.5%
American International Group, Inc.	0.5%
Total	**92.8%**

FUND PERFORMANCE (as of 12/31/2011)

	Cumulative Return	Average Annual Total Return
1-Year	-0.72%	-0.72%
Since Inception	10.36%	5.05%

US AGG BOND INDEX (as of 12/31/2011)

	Cumulative Return	Average Annual Total Return
1-Year	7.84%	7.84%
Since Inception	14.89%	7.19%

STATISTICS

YTD Return (12/31/11)	-0.72%
NAV (12/30/2011)	$9.91
12 Month Low-High	$9.42-$11.32
Net Assets ($Millions as of 12/30/11)	$298
30-Day SEC Yield	9.96%
Fiscal Year End	November 30
Fund Inception	12/31/2009
CUSIP	304871304
Fund Symbol	FOCIX

ANNUAL FUND OPERATING EXPENSES (1)

Gross Expense Ratio	1.02%
Fee Waiver and/or Expense Reimbursements	(0.25%)
Net Expense Ratio	0.77%

FEATURES

Minimum Initial Investment	$25,000
Minimum Retirement***	$25,000
Minimum Subsequent Investment	$2,500
Minimum Subsequent Retirement	$1,000
Minimum Automatic Investment Plan	$250

Performance Details

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 higher or lower than the performance information quoted herein. Performance figures assume reinvestment of dividends and capital gains and would have been lower without fee waivers in effect. Any questions you may have, including most recent month-end performance, can be answered by calling Shareholder Services at 1-866-202-2263.

(1) "Acquired Fund Fees and Expenses" are those fees and expenses incurred indirectly by the Income Fund as a result of investing in securities issued by one or more investment companies, including money market funds. The Advisor has contractually agreed to waive a portion of its management fees and/or pay Fund expenses (excluding taxes, interest, brokerage commissions, acquired fund fees and expenses, expenses incurred in connection with any merger or reorganization and extraordinary expenses such as litigation) in order to limit the net expenses of the Fund to 0.75% of the Fund's daily average net assets. The fee waiver/expense limitation became effective on March 30, 2011 and shall remain in effect until the effective date of the Fund's prospectus incorporating the Fund's audited financial statements for the Fund's fiscal year ending 2011. Without the expense limitation, the 30-Day SEC Yield would have been 9.70%."

*Cash and Cash Equivalents include investable cash and money market funds.

**Excludes cash and money market funds.

***The minimum initial investment may be waived by the Manager in its discretion.

The Barclays Capital U.S. Aggregate Bond Index ("US AGG BOND INDEX") represents securities that are SEC-registered, taxable, and U.S. dollar denominated. The index covers the U.S. investment grade fixed rate bond market, with index components for government and corporate securities, mortgage pass-through securities, and asset-backed securities. These major sectors are subdivided into more specific indices that are calculated and reported on a regular basis. It is not possible to invest directly in an unmanaged index. Prior to November 1st, 2008, this index was published by Lehman Brothers. The index is not meant to be indicative of the Fund's performance, asset composition, or volatility. Our results may differ markedly from those of US AGG BOND INDEX in either up or down market trends and interest rate environments. The performance of US AGG BOND INDEX does not reflect any management fees, transaction costs, or expenses.

The fund's investment objectives, risks, charges, and expenses should be considered carefully before investing. The prospectus contains this and other important information about the Fairholme Focused Income Fund, and it may be obtained by calling Shareholder Services at 1-866-202-2263 or visiting our website www.fairholmefunds.com. Read it carefully before investing.

Shares of the Fairholme Focused Income 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.

Fairholme Distributors, Inc. (01/12)

TRANSFER AGENT

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4400 Computer Drive
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FUND ADVISOR

Fairholme Capital Management, LLC
4400 Biscayne Boulevard
Miami, FL 33137

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The Fairholme Allocation Fund

INVESTMENT OBJECTIVE

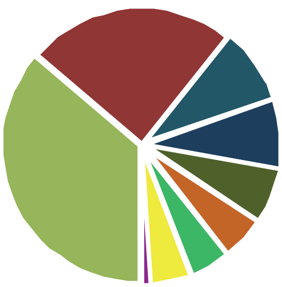
The Fairholme Allocation Fund seeks long-term total return from capital appreciation and income. The Fund attempts to achieve this investment objective by investing in a focused portfolio of investments in the equity, fixed-income and cash and cash-equivalent asset classes. The proportion of the Fund's portfolio invested in each asset class will vary from time to time based on Fairholme'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. The Fund seeks to capitalize on anticipated fluctuations in the financial markets by changing the mix of the Fund's holdings in the targeted asset classes. The Fund will use Fairholme's focused, multi-sector, multi-strategy, value-based approach. There is no guarantee that the fund will meet its objectives.

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

Please visit www.fairholmefunds.com for a prospectus, reports, and further details on the Fund's strategy.

TOP CATEGORIES

% of Total Portfolio as of 11/30/11



Surety Insurance	36.5%
Multi-Line Insurance	24.6%
Diversified Banks	8.9%
Diversified Holding Companies	8.1%
Cash and Cash Equivalents*	6.4%
Capital Markets	5.3%
Regional Banks	4.8%
Retail Department Stores	4.8%
Commercial Finance	1.0%

TOP HOLDINGS BY ISSUER***

as of 11/30/11

	%of Total Net Assets
MBIA, Inc.	36.5%
American International Group, Inc.	24.6%
Jeffries Group, Inc.	5.3%
Emigrant Bancorp, Inc.	4.8%
Sears Holdings Corp.	4.8%
Leucadia National Corp.	4.7%
Bank of America Corp.	4.4%
Berkshire Hathaway, Inc.	3.4%
Wells Fargo & Co.	3.2%
JPMorgan Chase & Co.	1.3%
Total	93.0%

FUND PERFORMANCE (as of 12/31/2011)

	Cumulative Return	Average Annual Total Return
1-Year	-14.00%	-14.00%
Since Inception	-14.00%	-14.00%

US AGG BOND INDEX (as of 12/31/2011)

	Cumulative Return	Average Annual Total Return
1-Year	7.84%	7.84%
Since Inception	7.84%	7.84%

STATISTICSSTATISTICS

Since Inception Return (as of 12/31/2011)	-14.00%
NAV (12/30/2011)	$8.60
12 Month Low-High	$6.98-$10.32
Net Assets ($Millions as of 12/30/2011)	$256
30-Day SEC Yield	-0.09%
Fiscal Year End	November 30
Fund Inception	12/31/2010
CUSIP	304871403

ANNUAL FUND OPERATING EXPENSES (1)

Gross Expense Ratio	1.00%
Fee Waiver and/or Expense Reimbursements	(0.25%)
Net Expense Ratio	0.75%

FEATURES

Minimum Initial Investment	$25,000
Minimum Retirement**	$25,000
Minimum Subsequent Investment	$2,500
Minimum Subsequent Retirement	$1,000

Performance Details

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. Performance would have been lower without fee waivers in effect. Current performance may be higher or lower than the performance information quoted herein. Performance figures assume reinvestment of dividends and capital gains, but does not reflect the effect of a 2% redemption fee, which is imposed on shares held less than 60 days. If it did, total returns would be reduced. Any questions you may have, including most recent month-end performance, can be answered by calling Shareholder Services at 1-866-202-2263.

S&P 500 INDEX (as of 12/31/2011)

	Cumulative Return	Average Annual Total Return
1-Year	2.11%	2.11%
Since Inception	2.11%	2.11%

(1) The Advisor has contractually agreed to waive a portion of its management fees and/or pay Fund expenses (excluding taxes, interest, brokerage commissions, acquired fund fees and expenses, expenses incurred in connection with any merger or reorganization and extraordinary expenses such as litigation) in order to limit the net expenses of the Fund to 0.75% of the Fund's daily average net assets. The fee waiver/expense limitation became effective on the effective date of the Fund's registration statement and shall remain in effect for at least one year after the effective date of the Prospectus and until the effective date of the Fund's Prospectus incorporating the Fund's audited financial statements for the Fund's fiscal year ending 2011. Without the expense limitation, the 30-Day SEC Yield would have been –0.36%.

*Cash and Cash Equivalents include investable cash and money market funds.

**The minimum initial investment may be waived by the Manager in its discretion.

***Excludes cash and money market funds.

Shares of the Fairholme Allocation 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.

The Barclays Capital U.S. Aggregate Bond Index ("US AGG BOND INDEX") represents securities that are SEC-registered, taxable, and U.S. dollar denominated. The index covers the U.S. investment grade fixed rate bond market, with index components for government and corporate securities, mortgage pass-through securities, and asset-backed securities. These major sectors are subdivided into more specific indices that are calculated and reported on a regular basis. It is not possible to invest directly in an unmanaged index. Prior to November 1st, 2008, this index was published by Lehman Brothers. The index is not meant to be indicative of the Fund's performance, asset composition, or volatility. Our results may differ markedly from those of US AGG BOND INDEX in either up or down market trends and interest rate environments. The performance of US AGG BOND INDEX does not reflect any management fees, transaction costs, or expenses.

The S&P 500 Index is a broad based measurement of changes in the stock market, is used for comparative purposes only, and is not meant to be indicative of the Fund's performance, asset composition or volatility. Given the wide scope of securities held by S&P 500, it should be inherently less volatile. Our results may differ markedly from those of the S&P 500 in either up or down market trends. The performance of the S&P 500 is shown with all dividends reinvested into the index and does not reflect any reduction in performance for the effects of transaction costs or management fees. Investors cannot invest directly in an index.

The Fund's investment objectives, risks, charges, and expenses should be considered carefully before investing. The prospectus contains this and other important information about the Fairholme Allocation Fund, and it may be obtained by calling Shareholder Services at 1-866-202-2263 or visiting our website www.fairholmefunds.com. Read it carefully before investing.

TRANSFER AGENT

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FUND ADVISOR

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FAIRHOLME CAPITAL MANAGEMENT, L.L.C.

Interview with Bruce Berkowitz

Moderator: Fred Fraenkel
February 8, 2012

EDITED FOR CLARITY AND ACCURACY

Fred: Bruce, it's great that we can do this today, because we've had a really tremendous response to asking our shareholders for questions. So we've taken all the questions and put them in the order of how often they were asked, and if it's okay with you, I'll just get right into it.

Bruce: Great, if you've got questions, hopefully, we'll have answers.

Fred: Okay. The most asked question was about Sears. People want to know what is the intrinsic value of Sears?

Bruce: That seems to be the $64 question, and it's hard for most to get a hold of it because of the different components. Everyone knows there's real estate, that they're a brand, and there's an online component. A lot of people don't realize that there's a service business with 12 million visits to homes every year, a warranty business on the products. Of course there's Sears Canada – mostly owned by Sears now. But the real interesting issue which people have to get their hands around is the long leases that Sears and Kmart have. You have to ask yourself the question, when does the long lease equal in value what ownership is.

So when you take into account the very long leases and just the nature of what it is to be an anchor in a mall, how you become an anchor and the terms and conditions of becoming an anchor in a mall, there's tremendous value. Quite a lot of work to get there, but when you add up all the values, including the long leases and the importance of anchors in malls, plus the brands, whether it's Lands' End online or the Sears websites that are doing reasonably well, you come up with a pretty big number. The number is multiples of what we think the current stock price is, but we'll let everybody on the outside figure out what the exact range is.

Fred: Given all those asset values, people also wanted to know whether you view this like a Berkshire Hathaway type of company?

Bruce: A lot of similarities. Warren Buffett, hedge fund manager, starts to invest heavily in a textile mill, Berkshire Hathaway. Over time, decides to call it a day as a fund manager, stays focused on Berkshire Hathaway. Tries to turn around the company, the entire company for the benefit of the employees. Eventually comes to the conclusion it can't happen, fixes what he can. Sells what he can't fix and moves on with insurance and becomes a conglomerate holding company, and the Berkshire that we know today.

If you take a look at Eddie Lampert in Sears from Kmart, so then the merger with Sears, then trying to fix the entire system. Recently announcing that it all can't be fixed, so that which can't be fixed will be sold. He’s going to rationalize it, and you can take a look at the cash flows. Whether it's his partnerships, the company’s recent purchase of more Sears, there's a pretty good analogy between the two. So can Sears become Eddie Lampert’s Berkshire Hathaway? Well, so far it looks that way. We’ll see.

Fred: Believe it or not, the second most asked question was about last year. Everybody knows that 2011 was a really tough year, and they want to know in retrospect, would you have done anything differently if you knew what you know now?

Bruce: In retrospect and in hindsight, yes, I'd do a lot differently. I'd go all to cash and I would have really slowed down the selling of the healthcare companies and the buying of the financials. With hindsight, of course I would do that. You know, we bought the healthcare companies when everyone thought they were going bankrupt because of Obamacare, and we knew that wouldn't be the case and we did reasonably well. But we sold too soon, because the financials became cheaper and because of the market’s belief that President Obama was going to destroy the financial system.

But the financials that we bought were cheap and they became much cheaper. Of course we buy cheap, and we bought more of those stocks cheaper. So yes, with hindsight, of course we’d do a lot. We’d be perfect. But given the events and given the fact that the business trends of every company that we purchased, that's all the financials that we purchased during that period have all turned positive since the time at which they'd been purchased. So it's going the way we expect it to go. It all looks great. The rest of the investment world has to start to be convinced that these are valuable franchises that are going to make money once they clear up the sort of one-time fixable problems they had from sort of the irrational exuberance of home ownership.

Fred: Sort of the follow-up to that, which they didn't ask, but I'll ask you is, are you happy with the whole portfolio the way it is now? Is this the portfolio that you want to take forward for the next couple of years?

Bruce: This is it. This is the kind of portfolio composition, business type that I had in the early '90s where I had my greatest performance, companies like Wells Fargo and others. It's what I know best. It's the industry that we're in. I mean, these companies, especially the financial services companies, are just dead center in what I believe to be my circle of competence. I've seen this act before. I've seen the play before. I've seen the cycle of financials. That's the one thing good about old age, you've seen it before and you know how it plays out. History may not be exact, but it does rhyme. I'm excited. I never thought I'd have another opportunity to really take advantage of the financial cycle. And we're going to do it, and hopefully this will be the year it shows.

Fred: AIG is our largest holding in the Fairholme Fund, and people wanted to know what the investment thesis is specifically on AIG. The backup question to that was why would you want to own a company that the government owns 77% of?

Bruce: We'll go with the latter question first. Why the government ownership is such a concern to long-term investors I don't know. To me it would be a positive. If you're truly a long-term investor, and you like to buy cheap and cheapen your value base, then the worst that could happen is you get to buy more at a cheaper price. That's the situation that we're in, and that's the reason why we bought more at a cheaper price, because of this fear. Going back, AIG, starting in this business, was the champion of the insurance business. A global enterprise, showing America how you can compete on a worldwide basis. Then you had it trading at five, six times book value, and then you have this tragedy that happens to the company, one step after another. It was Eliot Spitzer and then the recession and then the loss of management and the credit default swap issues. Then the taking of tremendous chunks of value from the company in order to repay the banks. And then the government taking its pound of flesh. A tragedy.

But the bottom line today is two core franchises are intact, Chartis and SunAmerica. The company has a tangible book value of $45 a share, going probably to $55 with the realization of tax-deferred assets, a few other areas. Earnings power of four dollars a share. So we're buying a company that was started in 1919 by C.V. Starr, at half of book value, that still has a significant franchise. And that's where we are. It's not more difficult than that, and it's a very common model that we're using for many of our companies. A company, a fixable problem. Fixable problem is covering up all that's good at the company. When the problem is fixed in total, and you see the normal cash flows of the business in a more normal environment, then it will be obvious to everyone the earnings power and the balance sheet strength of the company, and many of our other companies.

Fred: In the financials, in the banks and in the finance companies, going back to 2008 when you hadn't invested in them, you actually said you couldn't know what they owe, or what they owned, and it was difficult to know who owned them. But things have changed. Could you specify how that's happened?

Bruce: Well 2008 was really the beginning. It became obvious to everyone the significant problems from the real estate markets. We saw it, and Fairholme was always very financial services-oriented, and we got out of all the financials and started to watch what was going on. So we waited and waited for the companies to be recapitalized and restructured. Once they were recapitalized and restructured, and a couple of years went by, you can get an idea about the aging of the loans and contracts. Of course, investing is all about what you pay, what you give versus what you get. The prices just came down tremendously. So it got to the point where enough time went by where we believed we understood the loans, or we had an idea of a range of expectation and an understanding of the continued earnings power of the company. Plus they were recapitalized by the government.

So sterling balance sheet, continued earnings power. A quantifiable range of what it would take to fix the problems, mostly caused in 2006/2007 mortgages. With time you begin to know it. It's no different with insurance reserves and other areas. So you have today, a company with a book value of $20, a tangible book value of $12, $13. Earnings power of four dollars a share. And with a stock price seven, seven-and-a-half, wherever it may be.

Fred: Bank of America?

Bruce: Bank of America… it doesn't get any better when it comes to value investing. Investors tremendously overweight what recently happened to them, because of the pain and suffering that investors went through with the banks, and forget all of history, underweight all of history. Now banks, financials have cycles. We've just been through one, we're finishing one, and we're about to begin a new cycle for financial services.

Fred: One of the little soap operas in this cycle for us is that two of our portfolio companies are suing each other. Bank of America and MBIA. So some of the shareholders want to know your view of who's going to win.

Bruce: In fact, there are three; Bank of America, MBIA, and AIG. AIG's also suing Bank of America over issues. It all gets to representations and warranties, who promised what and what type of promise, what type of warranty. But the reason why we're on all sides of the fence is enough time has developed where you can see the reserves that the banks have, you can see the receivables that MBIA has, you've seen the development of the court cases over a couple of years. Enough time's gone by where Bank of America will end up owing MBIA some money, and most likely it's already been reserved for. Even if it isn't totally reserved for, Bank of America has such a significant cash flow coming in, pre-tax, pre-provisioning of $30 billion, $40 billion, even higher in a more normal environment, it's not an issue.

Whereas it's going to be a very big win for MBIA, it will be a significant amount of money for MBIA. This will allow them the capital that they're going to need to start new business again, especially after they get rid of another issue, which is what they call the transformation, in terms of the banks suing MBIA over the way they've changed their legal entities. So that has to get done, everybody has to settle up. You know, there's a lot of blame to go around for everyone. Banks have the blame, our government had blame, Freddie, Fannie, ACORN, people who actually signed loans and took the loans had a little bit of personal responsibility in there. The concept of home ownership went to an illogical extreme. It went from home ownership is a good idea to everyone should own a home. And that's what's led to the disaster, because greed kicked in and so on.

So that's going to be cleaned up, it's going to be taken care of. Everyone's going to be able to move on and get past this fixable problem. Then MBIA is going to absolutely be known for being the one guarantee agency that kept its word. Because unlike rating agencies, MBIA put their money where their mouth is. So if they guaranteed an issue, then they guarantee the buyers of that issue that they will take care of the timely payments of interest and principal. And they have. They've spent $5 billion, $6 billion of their money paying holders of asset-backed bonds without taking into account whether or not they illegally or erroneously purchased those bonds from the issuer. So they're going to fight it out with the issuers as to whether or not they're owed money, but they've kept their word to the holders of the bonds. When they start to do new business, people are going to remember that.

Fred: They were there.

Bruce: They were there, and they paid out, unlike the rating agencies which, you know, the ratings went down, but that was it. So it's been a long process, there's probably another year to go.

Fred: That's a complete answer, but it presupposes that MBIA net, in their suits with Bank of America, is going to win money. That's our operating assumption?

Bruce: Right. If you take a look at the reserves that Bank of America has for those types of lawsuits, if you look at Bank of America's settlements with other monolines and you look at what others have done in the industry to settle, it's clearly that money's going to be passed from Bank of America to MBIA on a net basis.

Fred: But you could have a settlement and have both stocks go up, because it's good for both?

Bruce: You should, because Wall Street hates uncertainty. What isn't going to be a big hit for Bank of America, could be a huge one for MBIA. So it clears the path at Bank of America to move forward, allows MBIA to move forward, and it takes away a lot of uncertainty. It's going to be a win for both.

Fred: Moving away from the portfolio, there are a bunch of questions that were Fairholme focused. The first one has to do with turnover in personnel and people want to know why, and they want to know is that good for the company?

Bruce: I think it is good for the company. People change, companies change. Sometimes the needs of the company and the needs of the individual no longer mesh. The environment changes. Our investment focus changes. At one point in time we'll need an expertise in one area, and maybe three years later, we will not need that expertise. There's a limited amount of dollars, so we always want to make sure we have the best people for the best task at-hand. In the end, for people that have been at Fairholme, I think Fairholme has been better for them being here. We're better for having new people come in, too, and that is the process. It seems to be okay at brokerage firms, at hedge funds, at other places, but for a mutual fund, there's this concept that everybody has to stay forever; it just doesn't make sense to me.

You know, our shareholders deserve the very best people for the current environment. And that's what we do, and hopefully our performance shows that.

Fred: Everyone's also aware that we had redemptions last year, and they're focused on knowing did the redemptions hurt our performance?

Bruce: We're long-term investors, so let's take this to an illogical extreme. Everyone leaves, I'm the last one left as a shareholder. And I end up with positions that are cheap, with billions of dollars of tax-deferred assets, and a great future. What I am trying to say is that for the long-term shareholder, the amount of redemptions should not matter. Could it potentially cause a lowering of price on a short-term basis? Yes. Do I think it has negatively affected short-term performance? No. I mean, there's a reason why we had $3 billion of cash that everyone was complaining about, and we utilized that cash for redemptions.

We've had to take other actions, but we have a more focused portfolio, because of that. So it has been to the long-term good of those of our shareholders who are still here. I still have to prove it, but the next couple of years we'll know.

Fred: Well, your extreme example is a good segue to another question that came up several times. People want to know if you still have most of your liquid net worth in the funds, and were you buying last year?

Bruce: Yes and yes. All of my family's liquid net worth is still in the funds and I pretty much bought every month of the year. So the answer is yes. I mean, that's what we do. We buy at X and we go to half X…

Fred: You're going to buy more.

Bruce: …not to buy more makes no sense.

Fred: Could you review the rationale for the three funds, because people still want to get that clear in their minds.

Bruce: The reason for three funds, well, let's back up. We had the Fairholme Fund and it grew and grew and grew. Then we went through the difficult period of 2008 where we had great relative performance, but there were shareholders who wanted an income-oriented fund. They said I don't want to leave Fairholme, I don't want to go somewhere else; why don't you have an income-oriented fund? So we created the Focused Income Fund for those shareholders. In fact, it was a good idea because during that difficult period when the credit markets froze up, there were some great fixed-income investments which may not necessarily have been perfect for the Fairholme Fund, but were outstanding for an income fund.

So we created as soon as possible, the next year, the Focused Income Fund. Then a year later, shareholders were saying, you know, you've gotten so big, you really can't take advantage of small quantity ideas anymore. It would be nice if there was a fund to take care of the small quantity ideas that really can make a big difference to the Fairholme Fund. That's why we created the Allocation Fund. That it would be small and we could really make a difference with small quantity ideas.

So if you look today at the three funds, you will see that we use different parts of the capital structure, and maybe even derivatives on the capital structure, for each of the funds.

In the case of Bank of America, we'll have the common equity in the Fairholme Fund where we have warrants on Bank of America in the Allocation Fund, because it's a small quantity idea. We would never be able to accumulate enough of it for the Fairholme Fund. We wouldn't have the liquidity. But for the Allocation Fund, it makes a lot of sense. Then if you take a look at Sears, Sears has some great bonds that are very high-yielding. We'll use Sears bonds in the Focused Income Fund, where we'll have Sears stock in the Fairholme

Fund. Or MBIA, believed to be a great investment, any fund can only have ten percent of MBIA's stock or of an issue of MBIA. So that in the case of the Fairholme Fund, it could never be a very big position, but it could be a very big position in the Allocation Fund. The bonds of MBIA we have used in the Focused Income Fund. So we do the work anyway, on a company, up and down the credit structure, from the bonds, right down to the preferred common equity. We try to utilize it where we can.

Fred: Use it appropriately?

Bruce: If it's a small quantity idea, it could really make a very big difference for the Allocation Fund. That's the reason for the three funds. Every time shareholders have a reasonable suggestion, we've tried to act on that suggestion.

Fred: The last question from shareholders is about your time. They want to know how do you spend your time, and has that changed much?

Bruce: My time is basically 80-20. Eighty percent on research, ideas, trying to destroy ideas, trying to come up with new ideas. Timely review of existing investments. And 20 percent on management and other activities. You know, a few years ago I was on two or three boards. But now I'm on the board of St. Joe, and people think that the chairmanship of St. Joe is taking up all of my time. That's not true. It's taken up time, it's been a very valuable experience in the same way my first directorship on a NYSE company was a very valuable experience, which I believe will help the funds in terms of what is gained.

At St. Joe, we went in as a shareholder because we wanted to make a difference. I promised that we would make a difference and then I would be gone. So today, we have a new board, a new management team. The bleeding has stopped at St. Joe, the balance sheet has been stabilized. The company is now in a position where they have the wherewithal to weather whatever the real estate environment is in the next few years, and to patiently wait for opportunity. And it's great. So it's been unbelievably educational, it's been interesting. I think that we've done well for the St. Joe shareholders and for Fairholme shareholders. And when I'm asked, I'll leave.

Fred: What else can you tell us?

Bruce: Twenty-eleven was a difficult year. It just didn't make sense. Fundamental values of our companies were improving, but the stock prices were being pummeled. Based upon correlated events, whether it was Europe or just the pain of the past, or very low interest rates. This tells me you have to have a long-term orientation. You can't follow the crowd, or as we say, you have to ignore the crowd. Just because you're right doesn't mean you're going to be immediately right. The value investor suffers from being a bit early. I mean, we shall see. So all in all, it tells me that given the stress of 2011, I think we have the shareholders who understand what we do. I believe there were those who did not understand what we do, those who chased performance, short-term performance.

Fred: Long gone?

Bruce: They're long gone. So we have the core shareholder base, with a core group of ideas that keep us in good stead, I think, for the next few years. If it's anything like a replay of the '90s that we witnessed, it should be quite good.

Fred: Thanks, Bruce.

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