

FAIRHOLME

Ignore the crowd.



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

Benjamin Graham

FAIRHOLME

Ignore the crowd.

PORTFOLIO MANAGER'S REPORT THE FAIRHOLME FUND

JANUARY 2013



*“Traditionally the investor has been the man with patience
and the courage of his convictions who would buy when the
harried or disheartened speculator was selling.”*

Benjamin Graham & David Dodd

Mutual fund investing involves risks, including loss of principal. The chart below covers the period from inception of The Fairholme Fund (December 29, 1999) to December 31, 2012. Past performance information to December 31, 2012, quoted below is unaudited and does not guarantee future results. The investment return and principal value of an investment in The Fairholme 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 below. Performance figures assume reinvestment of dividends and capital gains, but do not reflect a 2.00% redemption fee on shares redeemed within 60 days of purchase. 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 Fairholme Fund's performance, asset composition or volatility. Given the wide scope of securities held by the S&P 500, it should be inherently less volatile. The Fairholme Fund's performance may differ markedly from the performance 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. As reflected in its current prospectus dated March 29, 2012, The Fairholme Fund's Expense Ratio is 1.02%, which includes acquired fund fees and expenses of 0.02%. Acquired fund fees and expenses are those expenses incurred indirectly by The Fairholme Fund as a result of investments in securities issued by one or more investment companies, including, but not limited to, money market funds.

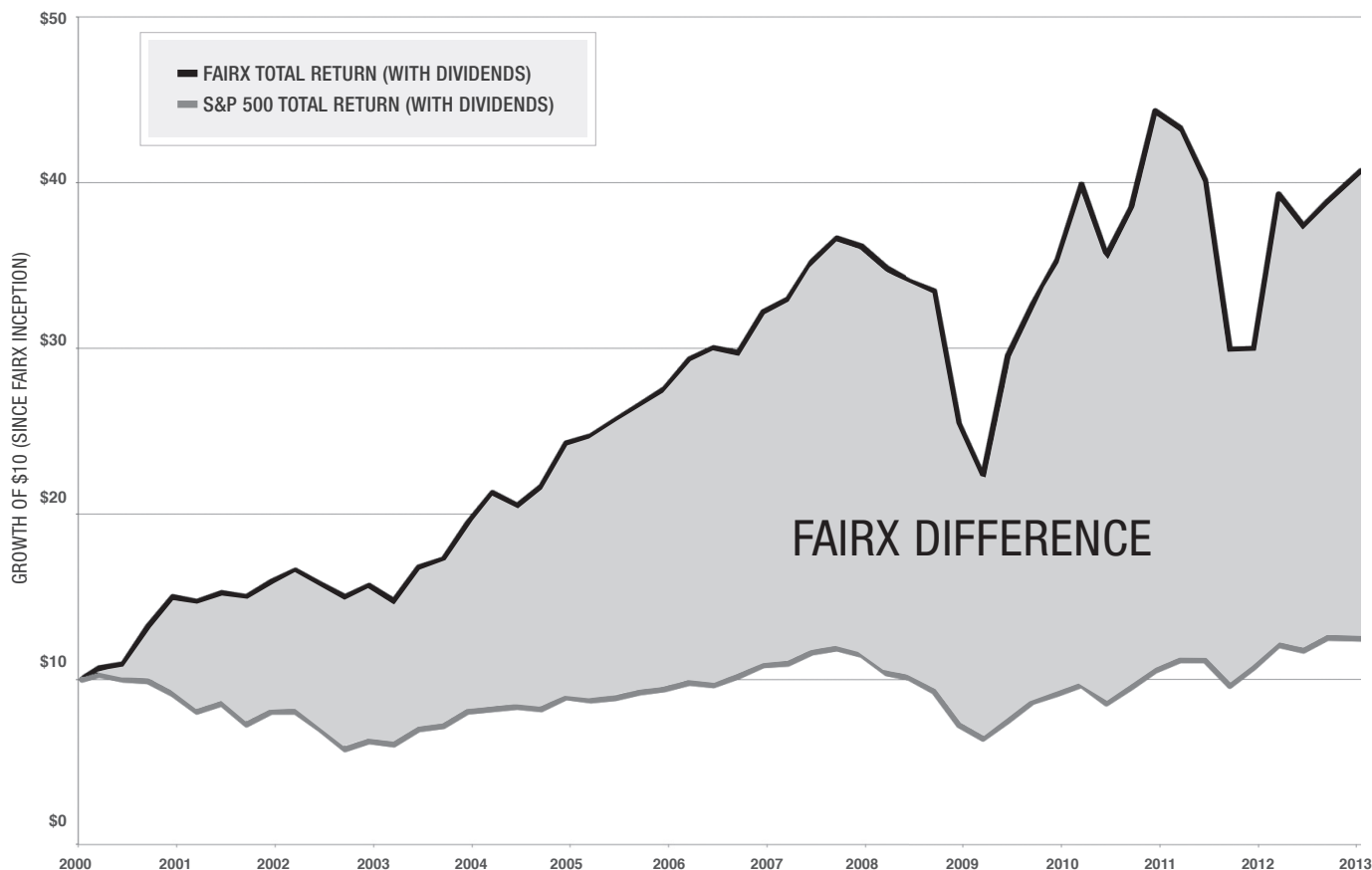
January 29, 2013

To the Shareholders and the Directors of The Fairholme Fund:

The Fairholme Fund (the "Fund") gained 35.81% versus 16.00% for the S&P 500 Index (the "S&P 500") in 2012. The following table compares the Fund's performance (after expenses) with that of the S&P 500 with dividends and distributions reinvested for the period ended December 31, 2012:

	One Year	Five Years	Ten Years	Since Inception (12/29/1999)
Cumulative:				
Fund	35.81%	12.55%	159.97%	306.49%
S&P 500	16.00%	8.59%	98.58%	24.39%
Annualized:				
Fund	35.81%	2.39%	10.03%	11.38%
S&P 500	16.00%	1.66%	7.10%	1.69%

A \$10.00 investment in the Fund at its inception has grown to \$40.65 (after expenses and assuming reinvestment of distributions) compared to \$12.44 for the S&P 500. The difference between those returns on a \$10.00 investment, more than anything, demonstrates how the Fund has outperformed the market (as represented by the S&P 500) over the long run. This difference is graphed below.



The Fund's average rolling 5-year return was 71.22% versus 16.01% for the S&P 500. The Fund has outperformed the S&P 500 in 94 of 97 5-year periods, calculated after each month end. The Fund's worst 5-year period return was (6.89)% versus (29.05)% for the S&P 500. In its best 5-year period, the Fund's return was 163.08% versus the S&P 500's best return of 105.13%.

Fund's Rolling 5-Year Period Return*			
	FAIRX	S&P	Relative Advantage
Best	+163.08% (3/2000-2/2005)	+105.13% (10/2002-9/2007)	+57.95%
Worst	(6.89)% (1/2007-12/2011)	(29.05)% (3/2004-2/2009)	+22.16%
Average	+71.22%	+16.01%	+55.21%

* Represents the percentage returns over a five-year rolling period (calculated after each month end) since inception through December 31, 2012.

To recite an old Merrill Lynch advertisement, "We're bullish on America." Our companies are capable of generating reasonable returns on equity and the companies sell for significantly less than our estimate of current equity values. In each case, earnings potential continues to be obfuscated by costs to fix past problems. Company equity values within the Fund were up 32% last year, but related market prices remain far below.

We had a great 2012, after a horrible 2011, and expect the Fund to reach new highs in the not too distant future. The U.S. is in its fourth year of recovery, housing prices are increasing but have yet to reach replacement values, unemployment is starting to decline, and interest rates remain at record lows. Our holdings are cheap relative to underlying equity values – as cheap as in the beginning of 2012. The Fund is highly focused on 5 companies representing nearly 80% of its net assets, with the knowledge that it is better to own more of your best ideas than your 10th best. Today, cash and equivalents stand at \$1.49 billion, about 19.7% of the Fund. Given current liquidity and the potential for performance dilution to shareholders, the Fund has determined to suspend the sale of shares to new investors after the last day of this February. The Fund will remain available for purchase to existing shareholders, may make exceptions to this suspension, and reserves the right to recommence sales to new investors in the future.

Fred Fraenkel and I now oversee risk analysis on a day-to-day basis utilizing a multi-path, independent process. For those who do not know Fred, we first worked together in 1990 at Lehman Brothers when he led 110 analysts around the globe to the #1 rank* and where a younger portfolio manager used him to critique work on the resurgence of financials after the commercial real estate collapse of that time. Two decades later, it's déjà vu all over again.

Onwards and upwards,



Bruce R. Berkowitz
 Managing Member
 Fairholme Capital Management

The Portfolio Manager's Report is not part of The Fairholme 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. A more formal Management Discussion and Analysis is included in the Annual Report. Opinions of the Portfolio Manager are intended as such, and not as statements of fact requiring attestation. All references to portfolio investments of The Fairholme Fund are as of the latest public filing of The Fairholme Fund with respect to such holdings at the time of publication, unless specified.

*The Institutional Investor All America Research Team

FAIRHOLME
Ignore the crowd.

The Fairholme Fund (FAIRX)
Seeking long-term growth of capital

ANNUAL REPORT 2012

MANAGED BY FAIRHOLME CAPITAL MANAGEMENT

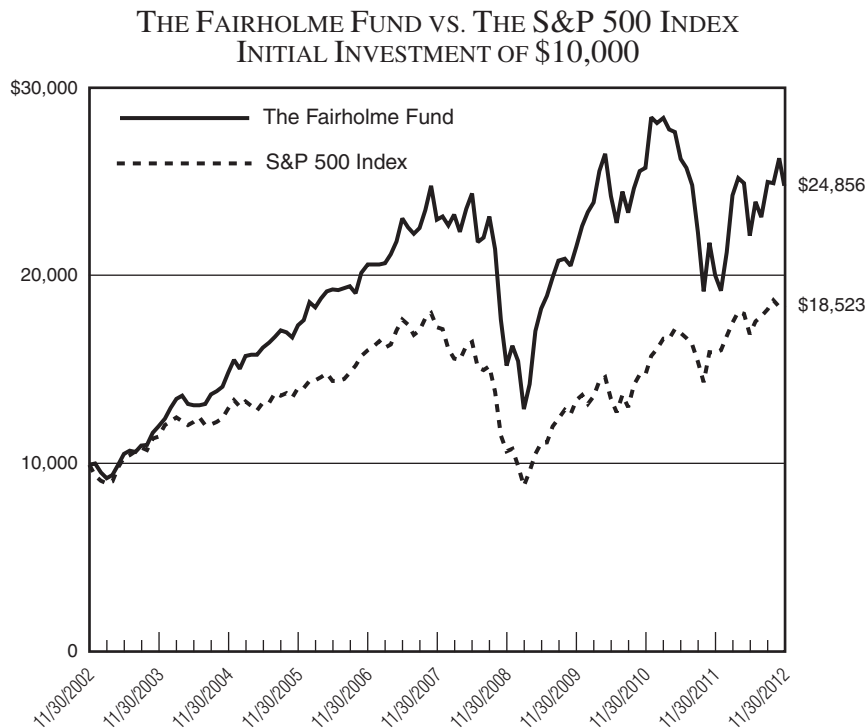
THE FAIRHOLME FUND

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THE FAIRHOLME FUND

FUND PERFORMANCE (Unaudited)
November 30, 2002 — November 30, 2012



The Fairholme Fund (the “Fund”) commenced operations on December 29, 1999. The chart above presents the performance of a \$10,000 investment for up to ten years to the latest fiscal year ended November 30, 2012.

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 higher or lower 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. Any questions you have regarding the performance data current to the most recent month-end can be obtained by calling Shareholder Services at 1-866-202-2263.**

Data for both the S&P 500 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 S&P 500 Index is a widely recognized, unmanaged index of 500 of the largest companies in the United States as measured by market capitalization and does not reflect any investment management fees or transaction expenses, nor the effects of taxes, fees or other charges.

THE FAIRHOLME FUND

MANAGEMENT DISCUSSION & ANALYSIS For the Fiscal Year Ended November 30, 2012

The Fairholme Fund (the “Fund”) shares outstanding and audited net asset value per share (“NAV”) at November 30, 2012, the end of the Fund’s fiscal year, and NAVs at other pertinent dates, were as follows:

	<u>11/30/2012 Shares Outstanding</u>	<u>11/30/2012 NAV (audited)</u>	<u>05/31/2012 NAV (unaudited)</u>	<u>11/30/2011 NAV (audited)</u>
Fund	233,953,597	\$29.89	\$26.70	\$25.10

At December 31, 2012, the unaudited NAV of the Fund was \$31.44. Performance figures below are shown for the Fund’s fiscal year ended November 30, 2012, and do not match calendar year figures for the period ended December 31, 2012, cited in the Portfolio Manager’s report.

	<u>Six Months</u>	<u>One Year</u>	<u>Five Years</u>	<u>Ten Years</u>	<u>Since Inception 12/29/1999</u>
Cumulative:					
Fund	11.95%	23.69%	7.90%	148.56%	286.45%
S&P 500	9.32%	16.13%	6.87%	85.23%	23.27%
Annualized:					
Fund		23.69%	1.53%	9.53%	11.02%
S&P 500		16.13%	1.34%	6.36%	1.63%

For the six months ended November 30, 2012, the Fund outperformed the S&P 500 Index (“S&P 500”) by 2.63 percentage points while over the last year the Fund outperformed the S&P 500 by 7.56 percentage points. From inception, the Fund outperformed the S&P 500 by 9.39 percentage points per annum or, on a cumulative basis, 263.18 percentage points over twelve years and eleven months.

Fairholme Capital Management, L.L.C. (the “Manager”) believes continuing economic recovery contributed to overall performance. However, the fact that securities increase or decline in value does not always indicate that the Manager believes these securities to be more or less or attractive — in fact, the Manager believes that some price increases present selling opportunities and some price declines present buying opportunities. 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 underlying corporation and its industry. However, certain strategies of the Manager in carrying out Fund policies may result in shorter holding periods.

In the opinion of the Manager, performance over short intervals is likely to be less meaningful than performance over longer periods. Investors are cautioned not to rely on short-term results. Further, shareholders should note that the S&P 500 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.

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, 2012, cash and cash equivalents (consisting of cash, commercial paper, deposit accounts, U.S. Treasury Bills, and money-market funds) represented

THE FAIRHOLME FUND

MANAGEMENT DISCUSSION & ANALYSIS (continued) For the Fiscal Year Ended November 30, 2012

11.2% of total assets. Since inception, the Fund has held liquid, low-risk securities or cash for periods without, in the Manager's view, negatively influencing performance, although there is no guarantee that future performance will not be negatively affected by Fund liquidity.

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 risky 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. The following charts show the top ten holdings by issuer and sector in descending order of net assets as of November 30, 2012.

The Fairholme Fund Top Ten Holdings by Issuer* (% of Net Assets)		The Fairholme Fund Top Ten Sectors (% of Net Assets)	
American International Group, Inc.	42.3%	Multi-Line Insurance	42.3%
Bank of America Corp.	11.5%	Diversified Banks	11.5%
Sears Holdings Corp.	8.5%	Cash and Cash Equivalents**	11.2%
General Growth Properties, Inc.	7.2%	Retail Department Stores	9.5%
The St. Joe Co.	6.9%	Real Estate Management & Development	7.8%
Leucadia National Corp.	3.9%	Real Estate Investment Trust	7.2%
CIT Group Inc.	3.2%	Diversified Holding Companies	3.9%
MBIA, Inc.	3.1%	Commercial Finance	3.2%
Sears Canada, Inc.	1.0%	Surety Insurance	3.1%
Howard Hughes Corp.	0.9%	Specialty Retail – Home Improvement	0.1%
	<u>88.5%</u>		<u>99.8%</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, since inception, such a strategy has negatively influenced short-term performance and there is no guarantee that future 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 Statement of Additional Information.

The Fund's Officers, the Board of Directors (the "Board" or the "Directors"), and 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. Mr. 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 10,487,264 shares at November 30, 2012. While there is no requirement that the Manager own shares of the Fund, such holdings are believed to help align shareholder interests.

Independent Fund Directors continue 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

THE FAIRHOLME FUND

MANAGEMENT DISCUSSION & ANALYSIS (continued)
For the Fiscal Year Ended November 30, 2012

significant personal investment in the Fund; the present constitution of Directors and policies; and current rules and regulations. Certain Directors and Officers of the Fund are also Officers of the Manager. Nevertheless, at November 30, 2012, 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 Directors affiliated with the Manager received no compensation for being Directors.

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 FUND

EXPENSE EXAMPLE

For the Six Month Period from June 1, 2012
through November 30, 2012 (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, redemption fees on Fund shares redeemed within 60 days of purchase, 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, 2012, and held for the entire six month period ending November 30, 2012.

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, 2012	Ending Account Value November 30, 2012	Annualized Expense Ratio	Expenses Paid During the Period June 1, 2012 Through November 30, 2012*
Actual	\$1,000.00	\$1,119.50	1.00%	\$5.30
Hypothetical (5% return before expenses)	\$1,000.00	\$1,020.00	1.00%	\$5.05

* Expenses are equal to the Fund’s annualized expense ratio, multiplied by the average account value over the period, multiplied by 183 days/366 days (to reflect the one-half year period).

THE FAIRHOLME FUND

SCHEDULE OF INVESTMENTS
November 30, 2012

Shares		Value	Shares		Value
	DOMESTIC EQUITY SECURITIES — 74.7%			DOMESTIC PREFERRED EQUITY SECURITIES — 0.0%	
	COMMERCIAL FINANCE — 3.2%			SPECIALTY RETAIL-HOME IMPROVEMENT — 0.0%	
6,068,829	CIT Group Inc. ^(a)	\$ 224,850,114			
	DIVERSIFIED BANKS — 11.5%		420,052	Orchard Supply Hardware Stores Corp., Preferred, Zero Coupon, Series A ^{(a)(d)}	\$ 756,094
81,607,015	Bank of America Corp.	804,645,168			
	DIVERSIFIED HOLDING COMPANIES — 3.9%			TOTAL DOMESTIC PREFERRED EQUITY SECURITIES (COST \$708,317)	<u>756,094</u>
12,229,050	Leucadia National Corp.	270,873,457			
	MULTI-LINE INSURANCE — 38.0%			WARRANTS — 12.4%	
80,280,825	American International Group, Inc. ^(a)	2,659,703,732		MULTI-LINE INSURANCE — 4.3%	
	REAL ESTATE MANAGEMENT & DEVELOPMENT — 6.9%		21,588,480	American International Group, Inc., Vested, Strike Price \$45.00, Expire 01/19/2021 ^{(a)(e)}	300,079,872
23,136,502	The St. Joe Co. ^{(a)(b)(c)(d)}	479,818,660			
	RETAIL DEPARTMENT STORES — 8.5%			REAL ESTATE INVESTMENT TRUSTS — 7.2%	
14,212,673	Sears Holdings Corp. ^(d)	597,074,393	40,634,357	General Growth Properties, Inc., Vested, Strike Price \$9.412, Expire 11/09/2017 ^{(a)(b)(c)(e)}	501,216,667
	SPECIALTY RETAIL-HOME IMPROVEMENT — 0.1%			REAL ESTATE MANAGEMENT & DEVELOPMENT — 0.9%	
592,993	Orchard Supply Hardware Stores Corp., Class A ^{(a)(d)}	4,595,696	1,896,270	Howard Hughes Corp., Vested, Strike Price \$50.00, Expire 11/09/2017 ^{(a)(b)(c)(e)}	62,518,505
	SURETY INSURANCE — 2.6%			TOTAL WARRANTS (COST \$351,676,339)	<u>863,815,044</u>
20,501,100	MBIA, Inc. ^{(a)(d)}	183,279,834			
	TOTAL DOMESTIC EQUITY SECURITIES (COST \$5,813,054,777)	<u>5,224,841,054</u>		Principal	
	FOREIGN EQUITY SECURITIES — 1.0%			DOMESTIC CORPORATE BONDS — 0.5%	
	CANADA — 1.0%			SURETY INSURANCE — 0.5%	
	RETAIL DEPARTMENT STORES — 1.0%			MBIA, Inc.	
6,087,327	Sears Canada, Inc. ^(a)	68,328,078	\$17,932,000	7.000%, 12/15/2025 ^(d)	14,166,280
	TOTAL FOREIGN EQUITY SECURITIES (COST \$65,108,224)	<u>68,328,078</u>	13,859,000	7.150%, 07/15/2027 ^(d)	11,017,905
			11,580,000	5.700%, 12/01/2034 ^(d)	9,206,100
					<u>34,390,285</u>
				TOTAL DOMESTIC CORPORATE BONDS (COST \$33,624,144)	<u>34,390,285</u>

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

THE FAIRHOLME FUND

SCHEDULE OF INVESTMENTS (continued)
November 30, 2012

<u>Principal</u>	<u>Value</u>	<u>Shares</u>	<u>Value</u>
U.S. GOVERNMENT OBLIGATIONS — 9.3%		MONEY MARKET FUNDS — 1.9%	
\$100,000,000	U.S. Treasury Bills 0.143%, 12/13/2012 ^(f)	136,597,492	Fidelity Institutional Money Market Funds - Money Market Portfolio, 0.180% ^(g)
100,000,000	U.S. Treasury Bills 0.096%, 01/24/2013 ^(f)	\$ 99,995,250	\$ 136,597,492
100,000,000	U.S. Treasury Bills 0.119%, 03/14/2013 ^(f)	99,985,675	TOTAL MONEY MARKET FUNDS
100,000,000	U.S. Treasury Bills 0.181%, 05/30/2013 ^(f)	99,976,200	(COST \$136,597,492)
100,000,000	U.S. Treasury Bills 0.203%, 06/27/2013 ^(f)	99,935,800	MISCELLANEOUS INVESTMENTS — 0.2% ^(h)
100,000,000	U.S. Treasury Bills 0.169%, 10/17/2013 ^(f)	99,922,800	(COST \$16,488,299)
50,000,000	U.S. Treasury Bills 0.163%, 11/14/2013 ^(f)	49,930,550	TOTAL INVESTMENTS — 100.0%
100,000,000	U.S. Treasury Bills 0.163%, 11/14/2013 ^(f)	99,841,700	(COST \$7,066,764,514)
TOTAL U.S. GOVERNMENT OBLIGATIONS			LIABILITIES IN EXCESS OF OTHER ASSETS — 0.0%
(COST \$649,506,922)	<u>649,587,975</u>		<u>(2,935,597)</u>
		NET ASSETS — 100.0%	<u>\$6,992,077,929</u>

^(a) Non-income producing security.

^(b) Security is deemed an illiquid security under procedures approved by the Directors.

^(c) Restricted or controlled security under procedures approved by the Directors. The value of these securities totals \$1,043,553,832, which represents 14.92% of the Fund's net assets. Information related to these securities is as follows:

<u>Acquisition Shares</u>	<u>Issuer</u>	<u>Acquisition Date(s)</u>	<u>Acquisition Cost</u>	<u>11/30/2012 Carrying Value Per Unit</u>
23,136,502	The St. Joe Co.	12/12/2007-10/13/2010	\$607,609,975	\$20.7386
40,634,357	General Growth Properties, Inc., Warrants, Vested, Strike Price \$9.412, Expire 11/09/2017	05/10/2010	—	12.3348
1,896,270	Howard Hughes Corp., Warrants, Vested, Strike Price \$50.00, Expire 11/09/2017	11/05/2010	—	32.9692

^(d) Affiliated Company. See Note 8.

^(e) Warrants have terms and conditions based on dividends paid and other events that may lower the strike price and raise the shares per warrant conversion ratio. Reported strike prices and conversion ratios are as of the date of this report. All share-to-warrant conversion ratios are currently 1:1, excluding the General Growth Properties, Inc. warrants, which on November 30, 2012 had a conversion ratio of 1:1.1157.

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

^(g) Annualized based on the 1-day yield as of November 30, 2012.

^(h) Represents previously undisclosed unrestricted securities, which the Fund has held for less than one year.

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

THE FAIRHOLME FUND

STATEMENT OF ASSETS & LIABILITIES November 30, 2012

Assets

Investments, at Fair Value:	
Unaffiliated Issuers (Cost — \$5,121,832,841)	\$5,695,098,564
Affiliated Issuers (Cost — \$1,944,931,673)	<u>1,299,914,962</u>
Total Investments, at Fair Value	
(Cost — \$7,066,764,514)	6,995,013,526
Receivable for Investments Sold	15,347,228
Receivable for Capital Shares Sold	1,524,314
Dividends and Interest Receivable	<u>1,305,109</u>
Total Assets	<u>7,013,190,177</u>

Liabilities

Payable for Capital Shares Redeemed	6,413,829
Payable for Investments Purchased	8,844,035
Accrued Management Fees	<u>5,854,384</u>
Total Liabilities	<u>21,112,248</u>

NET ASSETS

\$6,992,077,929

Net Assets Consist of:

Paid-In-Capital	\$7,250,541,308
Net Accumulated Realized Loss on Investments and Foreign Currency Related Transactions	(186,712,391)
Net Unrealized Depreciation on Investments and Foreign Currency Related Translations	<u>(71,750,988)</u>

NET ASSETS

\$6,992,077,929

Shares of Common Stock Outstanding* (\$0.0001 par value)	<u>233,953,597</u>
Net Asset Value, Offering and Redemption Price Per Share (\$6,992,077,929 / 233,953,597 shares)	<u>\$ 29.89</u>

* 700,000,000 shares authorized in total.

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

THE FAIRHOLME FUND

STATEMENT OF OPERATIONS

	For the Fiscal Year Ended November 30, 2012
Investment Income	
Interest — Unaffiliated Issuers	\$ 2,273,455
Interest — Affiliated Issuers	3,168,333
Dividends — Unaffiliated Issuers	14,492,822
Dividends — Affiliated Issuers	<u>95,239,107</u>
Total Investment Income	<u>115,173,717</u>
Expenses	
Management Fees	75,477,154
Other Expenses	<u>292,458</u>
Total Expenses	<u>75,769,612</u>
Net Investment Income	<u>39,404,105</u>
Realized and Unrealized Gain (Loss) on Investments and Foreign Currency Related Transactions	
Net Realized Gain (Loss) on Investments	
Unaffiliated Issuers	226,284,484
Affiliated Issuers	(34,322,124)
Net Realized Loss on Foreign Currency Related Transactions	(662)
Net Change in Unrealized Appreciation on Investments and Foreign Currency Related Transactions	<u>1,362,297,154</u>
Net Realized and Unrealized Gain on Investments and Foreign Currency Related Transactions	<u>1,554,258,852</u>
NET INCREASE IN NET ASSETS FROM OPERATIONS	<u><u>\$1,593,662,957</u></u>

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

THE FAIRHOLME FUND

STATEMENTS OF CHANGES IN NET ASSETS

	For the Fiscal Year Ended November 30, 2012	For the Fiscal Year Ended November 30, 2011
CHANGES IN NET ASSETS		
From Operations		
Net Investment Income (Loss)	\$ 39,404,105	\$ (33,469,437)
Net Realized Gain (Loss) on Investments and Foreign Currency Related Transactions	191,961,698	(366,929,655)
Net Change in Unrealized Appreciation (Depreciation) on Investments and Foreign Currency Related Translations	<u>1,362,297,154</u>	<u>(2,604,264,053)</u>
Net Increase (Decrease) in Net Assets from Operations	<u>1,593,662,957</u>	<u>(3,004,663,145)</u>
From Dividends and Distributions to Shareholders		
Net Investment Income	(213,247,996)	(195,136,284)
Net Realized Capital Gains from Investment Transactions	—	(838,210,865)
Return of Capital	<u>(63,552,375)</u>	<u>—</u>
Net Decrease in Net Assets from Dividends and Distributions	<u>(276,800,371)</u>	<u>(1,033,347,149)</u>
From Capital Share Transactions		
Proceeds from Sale of Shares	723,122,041	4,326,090,664
Shares Issued in Reinvestment of Dividends and Distributions	250,020,401	939,524,411
Redemption Fees	555,316	2,714,993
Cost of Shares Redeemed	<u>(3,313,776,781)</u>	<u>(10,062,106,880)</u>
Net Decrease in Net Assets from Shareholder Activity	<u>(2,340,079,023)</u>	<u>(4,793,776,812)</u>
NET ASSETS		
Net Decrease in Net Assets	(1,023,216,437)	(8,831,787,106)
Net Assets at Beginning of Year	<u>8,015,294,366</u>	<u>16,847,081,472</u>
Net Assets at End of Year	<u>\$ 6,992,077,929</u>	<u>\$ 8,015,294,366</u>
Distributions in Excess of Net Investment Income at End of Year	<u>\$ —</u>	<u>\$ (17,009,472)</u>
SHARES TRANSACTIONS		
Issued	25,564,197	127,523,200
Reinvested	10,652,155	27,554,666
Redeemed	<u>(121,560,995)</u>	<u>(328,478,267)</u>
Net Decrease in Shares	(85,344,643)	(173,400,401)
Shares Outstanding at Beginning of Year	<u>319,298,240</u>	<u>492,698,641</u>
Shares Outstanding at End of Year	<u>233,953,597</u>	<u>319,298,240</u>

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

THE FAIRHOLME FUND

FINANCIAL HIGHLIGHTS

	For the Fiscal Year Ended November 30,				
	2012	2011	2010	2009	2008
PER SHARE OPERATING PERFORMANCE					
NET ASSET VALUE, BEGINNING OF YEAR	\$25.10	\$34.19	\$28.90	\$20.95	\$32.30
Investment Operations					
Net Investment Income (Loss) ⁽¹⁾	0.15	(0.07)	0.33	0.28	0.13
Net Realized and Unrealized Gain (Loss) on Investments	5.55	(6.95)	5.22	8.20	(10.79) ⁽²⁾
Total from Investment Operations	5.70	(7.02)	5.55	8.48	(10.66)
Dividends and Distributions					
From Net Investment Income	(0.70)	(0.39)	(0.27)	(0.11)	(0.22)
From Realized Capital Gains	—	(1.69)	—	(0.43)	(0.48)
From Return of Capital	(0.21)	—	—	—	—
Total Dividends and Distributions	(0.91)	(2.08)	(0.27)	(0.54)	(0.70)
Redemption Fees⁽¹⁾	0.00 ⁽³⁾	0.01	0.01	0.01	0.01 ⁽²⁾
NET ASSET VALUE, END OF YEAR	\$29.89	\$25.10	\$34.19	\$28.90	\$20.95
TOTAL RETURN	23.69%	(22.10)%	19.37%	41.48%	(33.69)%
Ratio/Supplemental Data					
Net Assets, End of Year (in 000's)	\$6,992,078	\$8,015,294	\$16,847,081	\$10,558,010	\$6,696,139
Ratio of Expenses to Average Net Assets	1.00%	1.01% ⁽⁴⁾	1.00%	1.00%	1.01% ⁽⁵⁾
Ratio of Net Investment Income (Loss) to Average Net Assets	0.52%	(0.22)%	1.02%	1.14%	0.44%
Portfolio Turnover Rate	1.57%	43.95%	88.74%	71.09%	81.35%

⁽¹⁾ Based on average shares outstanding.

⁽²⁾ Redemption fees per share, which were initially reported as a component of net realized and unrealized gain (loss) on investments per share, were reclassified to conform to the current presentation and are separately reported.

⁽³⁾ Redemption fees represent less than \$0.01.

⁽⁴⁾ 0.01% is attributable to legal expenses borne by the Fund outside of the 1.00% management fee.

⁽⁵⁾ 0.01% is attributable to shareholder meeting expenses borne by the Fund outside of the 1.00% management fee.

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. 700,000,000 shares have been allocated to The Fairholme 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 provide long-term growth of capital. Under normal circumstances, the Fund seeks to achieve its investment objective by investing in a focused portfolio of equity and fixed-income securities. The proportion of the Fund’s assets invested in each type of asset class will vary from time to time based upon Fairholme Capital Management, L.L.C.’s (the “Manager”) assessment of general market and economic conditions. The Fund may invest in, and may shift frequently among, the asset classes and market sectors. The equity securities in which the Fund may invest include common and preferred stock (including convertible preferred stock), partnership interests, business trust shares, interests in real estate investment trusts (“REITs”), rights and warrants to subscribe for the purchase of equity securities, and depository receipts. The Fund may invest in equity securities without regard to the jurisdictions in which the issuers of the securities are organized or situated and without regard to the market capitalizations or sectors of such issuers. The fixed-income securities in which the Fund may invest include U.S. corporate debt securities, non-U.S. corporate debt securities, bank debt (including bank loans and participations), U.S. government and agency debt securities, short-term debt obligations of foreign governments, and foreign money market instruments. Except for its investments in short-term debt obligations of foreign governments, the Fund may invest in fixed-income securities regardless of maturity or the rating of the issuer of the security. The Fund may also invest in “special situations” to achieve its objective. “Special situation” investments may include equity securities or fixed-income securities, such as corporate debt, which may be in a distressed position as a result of economic or company specific developments. Although the Fund normally holds a focused portfolio of equity and fixed-income 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. The Manager serves as investment adviser to the Fund.

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

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 generally determines its net asset value as of approximately 4:00 p.m. Eastern Time 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. 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. As of November 30, 2012, equity investments of The St. Joe Co. valued at \$479,818,660 (6.86% of net assets) in the Fund

are fair valued by the Manager due to a trading restriction. The value is calculated by applying a discount to the official closing price on the day of valuation.

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. As of November 30, 2012, 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, 2012, 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 either Level 2 or Level 3 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 of securities not valued by these and other TPPS. 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, prices will be sought from another pricing service or from a broker/dealer that trades that security or similar securities.

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 FUND

NOTES TO FINANCIAL STATEMENTS (continued)
November 30, 2012

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 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, 2012 is as follows:

	Valuation Inputs		
	Level 1 – Quoted Prices	Level 2 – Other Significant Observable Inputs	Total Fair Value at 11/30/2012
ASSETS:			
INVESTMENTS (Fair Value):			
Domestic Equity Securities			
Real Estate Management & Development	\$ —	\$ 479,818,660	\$ 479,818,660
Other*	4,745,022,394	—	4,745,022,394
Foreign Equity Securities*	68,328,078	—	68,328,078
Domestic Preferred Equity Securities*	756,094	—	756,094
Warrants			
Multi-Line Insurance	300,079,872	—	300,079,872
Real Estate Investment Trusts	—	501,216,667	501,216,667
Real Estate Management & Development	—	62,518,505	62,518,505
Domestic Corporate Bonds	—	34,390,285	34,390,285
U.S. Government Obligations	—	649,587,975	649,587,975
Money Market Funds	136,597,492	—	136,597,492
Miscellaneous Investments	16,697,504	—	16,697,504
TOTAL INVESTMENTS	\$5,267,481,434	\$1,727,532,092	\$6,995,013,526

* 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, 2012.

The following is a reconciliation of Level 3 investments for which significant unobservable inputs were used to determine fair value:

	Assets: Investments (Fair Value)		
	Warrants		
	Real Estate Investment Trusts	Real Estate Management & Development	Total Level 3 Investments
Balance as of 11/30/2011	\$ 339,268,437	\$ 35,943,608	\$ 375,212,045
Change in unrealized appreciation	—	—	—
Purchases	—	—	—
Sales	—	—	—
Transfers into Level 3 ⁽¹⁾	—	—	—
Transfers out of Level 3 ⁽¹⁾	(339,268,437)	(35,943,608)	(375,212,045)
Balance as of 11/30/2012	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>

⁽¹⁾ The Fund's policy is to recognize transfers into and transfers out of Level 3 as of the beginning of the reporting period. As of November 30, 2011, the Fund used certain significant unobservable inputs in determining the value of these investments. As of November 30, 2012, the Fund used observable inputs in determining the value of the same investments. As a result, the investments transferred from Level 3 to Level 2 in the disclosure hierarchy.

Recent Accounting Standards: In December 2011, FASB issued ASU No. 2011-11, "Disclosures about Offsetting Assets and Liabilities". ASU 2011-11 requires disclosures to make financial statements that are prepared under U.S. GAAP more comparable to those prepared under International Financial Reporting Standards. The new disclosure requirements mandate that entities disclose both gross and net information about instruments and transactions eligible for offset in the statement of assets and liabilities as well as instruments and transactions subject to an agreement similar to a master netting arrangement. In addition, ASU 2011-11 requires disclosure of collateral received and posted in connection with master netting agreements or similar arrangements. New disclosures are required for annual reporting periods beginning on or after January 1, 2013 and interim periods within those annual periods. Management is evaluating the impact of ASU 2011-11 on the financial statements and disclosures.

Warrants: The Fund's investments in warrants as of November 30, 2012, are presented within the Schedule of Investments.

The Fund's warrant positions during the fiscal year ended November 30, 2012 had an average monthly market value of approximately \$732,952,141.

As of November 30, 2012, the value of warrants with equity risk exposure of \$863,815,044 is included with Investments at Fair Value on the Statement of Assets and Liabilities. For the fiscal year ended November 30, 2012, the effect of the net change in unrealized appreciation of warrants with equity risk exposure held of \$356,481,502 is included with the Net Change in Unrealized Appreciation on Investments and Foreign Currency Related Translations on the Statement of Operations.

Dividends and Distributions: The Fund records dividends and distributions to shareholders on the ex-dividend date. The Fund intends to distribute substantially all of its net investment income (if any) as dividends to its shareholders on an annual basis in 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.

Redemption Fee: The Fund assesses a 2% fee on the proceeds of the Fund shares that are redeemed within 60 days of their purchase. The redemption fee is paid to the Fund as applicable, for the benefit of remaining shareholders and is recorded as paid-in capital. The redemption fees retained by the Fund during the fiscal years ended November 30, 2012 and November 30, 2011 amounted to \$555,316 and \$2,714,993, respectively.

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, other brokerage fees, and security registration expenses 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, except for commissions, brokerage fees, and other transaction costs, taxes, interest, litigation expenses, and related expenses, and other extraordinary expenses.

The Manager earned \$75,477,154 from the Fund for its services during the fiscal year ended November 30, 2012.

Certain Directors and Officers of the Fund are also Members and Officers of the Manager.

Note 4. Investments

For the fiscal year ended November 30, 2012, aggregated purchases and sales of investment securities other than short-term investments were as follows:

<u>Purchases</u>	<u>Sales</u>
\$107,055,590	\$2,798,946,656

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.

THE FAIRHOLME FUND

NOTES TO FINANCIAL STATEMENTS (continued)
November 30, 2012

For U.S. federal income tax purposes, the cost of securities owned, gross unrealized appreciation, gross unrealized depreciation, and net unrealized depreciation of investments at November 30, 2012 were as follows:

<u>Cost</u>	<u>Gross Unrealized Appreciation</u>	<u>Gross Unrealized Depreciation</u>	<u>Net Unrealized Appreciation (Depreciation)</u>
\$7,071,524,474	\$1,042,545,373	\$(1,119,056,321)	\$(76,510,948)

The difference between book basis and tax basis net unrealized depreciation, if any, is primarily attributable to the tax deferral of losses on wash sales.

The Fund's tax basis capital gains are determined at the end of each fiscal year. As of November 30, 2012, the components of distributable earnings on a tax basis were as follows:

Accumulated Capital Loss Carryforwards	\$(181,952,431)
Net Unrealized Depreciation on Investments and Foreign Currency Related Transactions	<u>(76,510,948)</u>
Total	<u><u>\$(258,463,379)</u></u>

At November 30, 2012, the Fund utilized capital loss carryforwards of \$176,062,509. The Fund has \$181,952,431 of net capital loss carryforwards available to reduce future required distributions of net capital gains to shareholders through 2019.

The Manager has analyzed the Fund's tax positions taken on federal income 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 the prior year) are subject to examination by the Internal Revenue Service and state departments of revenue.

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 was as follows:

	<u>For the Fiscal Year Ended November 30, 2012</u>	<u>For the Fiscal Year Ended November 30, 2011</u>
Dividends and Distributions paid from:		
Ordinary Income*	\$213,247,996	\$ 199,071,043
Long-Term Capital Gain	—	834,276,106
Return of Capital	<u>63,552,375</u>	<u>—</u>
	<u><u>\$276,800,371</u></u>	<u><u>\$1,033,347,149</u></u>

* Inclusive of short-term capital gains

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 were primarily due to the tax treatment of currency gains and losses for the Fund and recharacterization of distributions for the Fund reclass of capital gains and losses for passive foreign investment companies for the Fund. As of November 30, 2012, the Fund recorded the following reclassifications to increase (decrease) the accounts listed below:

Accumulated Undistributed Net Investment Income	\$ 254,405,738
Net Accumulated Realized Gain	(14,790,854)
Paid-in-Capital	(239,614,884)

Note 8. Transactions in Shares of Affiliates

Portfolio companies in which the Fund owns 5% or more of the outstanding voting securities of the issuer are considered affiliates of the Fund. The aggregate fair value of all securities of affiliates held in the Fund as of November 30, 2012 amounted to \$1,299,914,962, representing 18.59% of the Fund's net assets.

Transactions in the Fund during the fiscal year ended November 30, 2012 in which the issuer was an affiliate are as follows:

	November 30, 2011	Gross Additions	Gross Deductions	November 30, 2012			
	Shares/ Par Value	Shares/ Par Value	Shares/ Par Value	Shares/ Par Value	Fair Value	Realized Gain (Loss)	Investment Income
CIT Group Inc. ^(a)	16,358,129	—	10,289,300	—	\$ —	\$(30,554,901)	\$ —
MBIA, Inc.	20,501,100	—	—	20,501,100	183,279,834	-	—
Orchard Supply Hardware Stores Corp., Class A ^(b)	—	641,893	48,900	592,993	4,595,696	(3,627,929)	—
Sears Holdings Corp.	14,212,673	—	—	14,212,673	597,074,393	—	95,239,107
The St. Joe Co.	23,136,502	—	—	23,136,502	479,818,660	—	—
Orchard Supply Hardware Stores Corp., Preferred, Zero Coupon, Series A ^(b)	—	641,893	221,841	420,052	756,094	(139,294)	—
MBIA, Inc. 7.000%, 12/15/2025	\$17,932,000	\$ —	\$ —	\$17,932,000	14,166,280	—	1,396,153
MBIA, Inc. 7.150%, 07/15/2027	\$13,859,000	\$ —	\$ —	\$13,859,000	11,017,905	—	1,060,492
MBIA, Inc. 5.700%, 12/01/2034	\$11,580,000	\$ —	\$ —	\$11,580,000	9,206,100	—	711,688
Total					<u>\$1,299,914,962</u>	<u>\$(34,322,124)</u>	<u>\$98,407,440</u>

^(a) Company is not an "affiliated company" as of November 30, 2012, but remains an investment in the Fund's portfolio. Affiliated realized loss is shown for transactions that occurred through the date the Fund no longer owned 5% or more of the outstanding voting securities of the issuer.

^(b) Security received in spin-off from Sears Holdings Corp. and was not held in the portfolio at November 30, 2011.

Note 9. 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 enters 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 Fund:

We have audited the accompanying statement of assets and liabilities, including the schedule of investments, of The Fairholme Fund (the "Fund"), as of November 30, 2012, 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, 2012, by correspondence with the custodian and brokers; where replies were not received from brokers, we performed other auditing procedures. 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 Fund as of November 30, 2012, the results of its operations, the changes in its net assets, 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, 2013

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 with the Company	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 54	Director, President	Mr. Berkowitz has served as a Director 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 65	Director	Mr. Alvarez has served as a Director of the Company since May 19, 2008.	Executive Chairman of Greenberg Traurig, LLP since 2010; Chief Executive Officer of Greenberg Traurig, LLP from October 1997 to 2010.	3	Chairman, Board of Directors, Mednax, Inc.; Co-Leading Director, Watsco, Inc.; Vice Chairman, Knight Foundation; Director, The St. Joe Co.
Independent Directors^					
Terry L. Baxter Age 67	Director	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 71	Director	Mr. Frank has served as a Director of the Company since May 7, 2007.	Vice Chairman, Chief Operating Officer and Director, Carnival Corporation & plc.	3	Director, Steamship Mutual Trust; Director, New World Symphony; Director, The St. Joe Co.
Avivith Oppenheim, Esq. Age 62	Director	Ms. Oppenheim has served as a Director of the Company since December 15, 1999.	Attorney-at-Law.	3	None.
Leigh Walters, Esq. Age 66	Director	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.

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 63^	Vice President	Mr. Fraenkel has served as Vice President of the Company since January 2013.	Chief Research Officer, Fairholme Capital Management, L.L.C. since October 2011; Vice Chairman Beacon Trust Company from 2008 to 2011; Chairman of Millennium 3 Capital from 2000 to 2008.
Wayne Kellner Age 43	Treasurer	Mr. Kellner has served as Treasurer of the Company since March 2012.	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 56	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; Managing Director and former Chief Financial Officer of Colliers-Seeley, Inc. from 2004 to February 2007.

† 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.

^ Fred Fraenkel was elected Vice President in January 2013 and thus did not serve as an officer of the Company during the period covered by this report.

Approval of Investment Management Agreement (unaudited)

At its meeting on October 18, 2012, the Board of Directors of Fairholme Funds, Inc. (the “Company”) approved the renewal of the investment management agreement between the Company, on behalf of The Fairholme 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 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 information concerning the Manager’s commitment to the Fund as evidenced by the current share ownership in the Fund by management/owners of the Manager. The Directors considered information describing the Manager’s compliance policies and procedures, including 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 the services provided by the Manager to the Fund with the services provided by the Manager to certain of its other advisory accounts, as 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 also considered a third party report comparing the Fund’s investment performance with the investment performance of similarly situated mutual funds. The report for the Fund reflected the performance of the Fund and the similarly situated mutual funds for the 1-year, 3-year, 5-year, 10-year and since Fund inception periods ended August 31, 2012.

C. Management Fee and Expense Ratio

The Directors considered information concerning the Fund’s management fee and expense ratio, including a third party report comparing the Fund’s management fee and most recent expense ratio to the advisory fees and expense ratios of other similarly situated mutual funds. The Directors noted that the Fund’s management fee covers many of the operating and other expenses of the Fund. The Directors noted that the Fund’s expense ratio for its latest full fiscal year was lower than the median expense ratios 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 and strategies and asset size. They also considered information regarding the Manager’s payment (in some cases from its resources) of certain expenses for the benefit of the Fund, including distribution expenses and 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 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 asset level, overall expense ratio, performance and the services provided by or through the Manager. The Directors concluded that the Manager's estimated profitability was not such as to prevent them from approving the renewal of the agreement.

E. Economies of Scale

The Directors considered information concerning economies of scale for the Fund, including the Fund's current assets. The Directors concluded 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, 2012, 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 visiting our website at 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).

Shareholder Tax Information (unaudited)

The Fund reported \$213,247,996 of total distributions paid during the fiscal year ended November 30, 2012, as ordinary income distributions.

The information below is reported from 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 2013 to determine the calendar year amounts to be included on their 2012 tax returns. Shareholders should consult their own tax advisors.

Please note that, for the fiscal year ended November 30, 2012, the respective percentages of ordinary income distributions paid by the Fund were reported as follows:

Distribution Period November 30, 2012	
Qualified Dividend Income for Individuals	33.11%
Dividends Qualifying for the Dividends Received Deduction for Corporations	33.11%
Qualifying Interest Income	5.32%
Qualifying Short-term Gain	—
U.S. Treasury Securities	0.09%

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 presented 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

Avivith Oppenheim, Esq.

Leigh Walters, Esq.

Investment Manager

FAIRHOLME CAPITAL MANAGEMENT, L.L.C.

4400 Biscayne Boulevard

Miami, FL 33137

Transfer Agent, Fund Accountant and Administrator

BNY MELLON INVESTMENT SERVICING (US) INC.

760 Moore Road

King of Prussia, PA 19406

Custodian

THE BANK OF NEW YORK MELLON

1 Wall Street

New York, NY 10286

Independent Registered Public Accounting Firm

DELOITTE & TOUCHE LLP

1700 Market Street

Philadelphia, PA 19103

Legal Counsel

SEWARD & KISSEL LLP

901 K Street NW

Washington, DC 20001

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