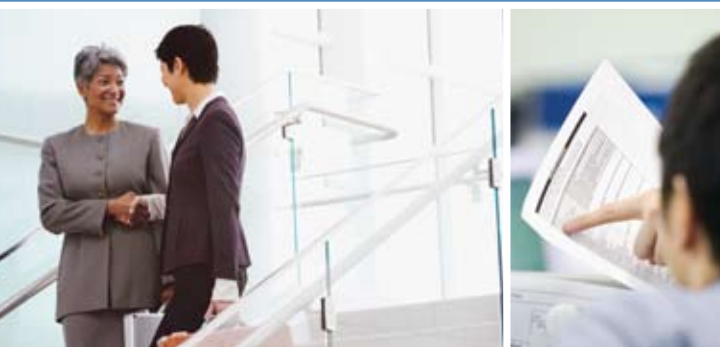


# Diversification

UNDERSTANDING THE BASICS



FOR INVESTORS



Smart move.™



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## Why diversify?

Successful investors and investment professionals know that diversification is the key to a balanced portfolio and a primary strategy for managing risk.

Spreading your money among different asset classes and types of investments helps reduce the impact on your portfolio of any one poorly performing investment. It acts to mitigate the effects of market extremes – both lows and highs – which diminishes risk. Diversifying your portfolio doesn't guarantee a profit or protect you from a loss, but it does offer the potential for more consistent long-term returns.

The best part is that for all its positive points, diversification – as you will see in the next several pages – is neither complicated nor difficult.

## Building blocks of diversification

Diversification entails more than just owning a large number of investments. To be effective, your investments need to include securities that behave differently from each other under various market and economic conditions.

Equities and fixed-income securities, i.e., stocks and bonds, are the major building blocks of a diversified portfolio. These two asset classes historically have complemented each other in performance and risk attributes. A modest percentage of cash-equivalent short-term investments, such as CDs, may also be used to round out portfolio diversification.



## Fixed-income

Fixed-income securities, or bonds, typically have more moderate performance highs and lows than stocks and therefore carry lower risk. Bond performance is vulnerable to changes in interest rates, rising and falling inflation, and credit risk. With their lower risk, bonds typically offer lower returns.

## Equities

Equities, or stocks, typically are more volatile than bonds. Because of their wider range of performance highs and lows over any given period, stocks carry higher risk than bonds. Stock performance is sensitive to the profitability of individual companies and prosperity of particular industries. The trade-off for higher risk is that stocks offer potentially higher returns.

International stocks, especially those of companies in emerging markets, may incur greater risk than domestic U.S. stocks because of their exposure to potentially more magnified currency exchange rate, economic, and political risks.

By including securities from both fixed-income and equity asset classes among your investments, you are able to take advantage of a broader range of investing opportunities.

## The cornerstone of investing

If you could know in advance which securities are going to be the top performers, there would be no need to diversify. But history shows that it's not possible to predict which securities will be the winners from year to year.

During the past 10 years, for example, the top-performing group of securities has switched randomly among U.S. stocks, international stocks, and U.S. bonds.

### MARKET CYCLES:

#### Calendar year returns, 1998–2007

- Fixed-Income (Lehman Brothers U.S. Aggregate Index)
- Domestic Equity (S&P 500 Index)
- International Equity (MSCI EAFE Index)

|      | Best ← | → Worst |         |
|------|--------|---------|---------|
| 1998 | 28.58% | 20.33%  | 8.67%   |
| 1999 | 27.30% | 21.04%  | -0.83%  |
| 2000 | 11.63% | -9.11%  | -13.96% |
| 2001 | 8.42%  | -11.88% | -21.21% |
| 2002 | 10.27% | -15.66% | -22.10% |
| 2003 | 39.17% | 28.70%  | 4.11%   |
| 2004 | 20.70% | 10.87%  | 4.34%   |
| 2005 | 14.02% | 4.91%   | 2.43%   |
| 2006 | 26.86% | 15.80%  | 4.33%   |
| 2007 | 11.63% | 6.96%   | 5.49%   |

Source: FMR LLC.

**Past performance is no guarantee of future results.**

**It is not possible to invest directly in an index.**

**Index performance is not meant to represent that of any Fidelity mutual fund.**

Please see last page for index definitions.



The most realistic strategy is to own investments in several categories to improve the odds of benefiting from good performance whenever and wherever it occurs.

## Strategies for diversification

In order to create a strategically balanced investment mix, there are two levels of diversification to consider:

- **Diversifying among asset groups** – spreading investments among asset classes
- **Diversifying within each asset group** – spreading investments among asset subgroups



# Diversify among asset groups

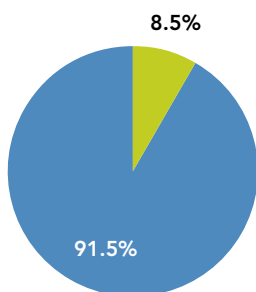
## Asset allocation

Start with asset allocation, the most fundamental step in portfolio diversification. To get an idea of how important asset allocation is, consider the fact that 91.5% of investment performance is attributable to asset allocation decisions.<sup>1</sup>

### ASSET ALLOCATION VS. SECURITY SELECTION<sup>1</sup>

Impact on variability of performance

- Asset Allocation
- Security Selection, Market Timing, and Other



1. Brinson, Hood and Beebower, "Determinants of Portfolio Performance," *Financial Analysts Journal*, July–August 1986; Brinson, Singer and Beebower, "Determinants of Performance II: An Update," *Financial Analysts Journal*, May–June 1991.

Failing to diversify properly could mean not only losing money when a particular segment of the market deteriorates, but also losing out when it improves. By diversifying across asset groups, you help mitigate portfolio losses and thus enable yourself to recover more quickly when the market rebounds.

Varying the proportions of asset groups creates different risk/return scenarios. Your objective in asset allocation is to determine the balance that best meets your financial goals while staying within your risk comfort zone.

## Determining your target asset mix

Your target asset mix is based on your time horizon, financial situation, and risk tolerance.

Ask yourself:

- How much time before I will need the money for my goal?
- How much can I afford to invest regularly?
- How much would I have to save each year to reach my financial target?
- How comfortable am I in taking on risk – will I be able to weather short-term market declines?

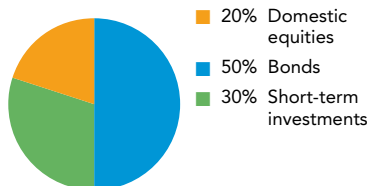
First, the longer your investing timeline, the more aggressive you can afford to be, since market ups and downs tend to level out over time, reducing volatility and investment risk.

Also, investments that are too conservative may not keep pace with inflation, shortening the productive life of your assets.

## Allocating your portfolio assets

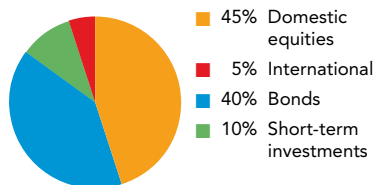
Fidelity believes that the essential first step to a properly diversified portfolio is to include a wide variety of investments. The following target asset mixes illustrate four investment strategies.

### Conservative target asset mix



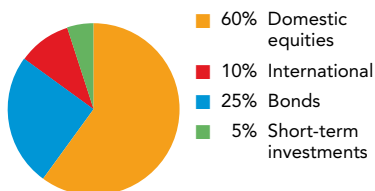
This target asset mix may be appropriate for investors who want to minimize fluctuations in market values by taking an income-oriented approach with some potential for capital appreciation.

### Balanced target asset mix



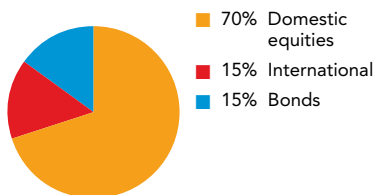
This target asset mix may be appropriate for investors who want the potential for capital appreciation and some income and who can withstand moderate fluctuations in market value.

### Growth target asset mix



This target asset mix may be appropriate for investors who have a preference for growth and who can withstand significant fluctuations in market value.

### Aggressive growth target asset mix

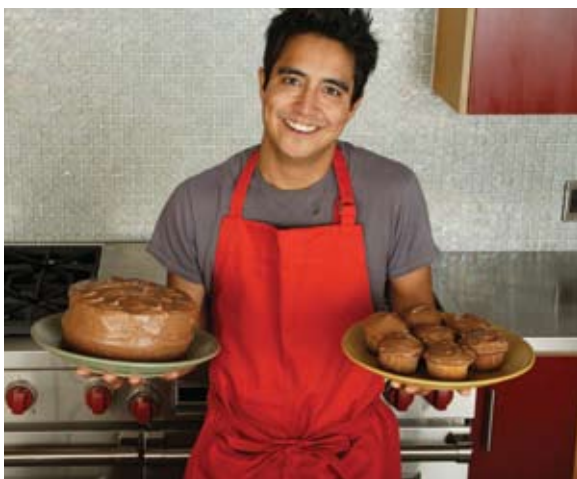


This target asset mix may be appropriate for investors who seek aggressive growth and who can tolerate wide fluctuations in market value, especially over the short term.

The purpose of the target asset mixes is to show how target asset mixes may be created with different risk and return characteristics to help meet a participant's goals. You should choose your own investments based on your particular objectives and situation. Remember that you may change how your account is invested. Be sure to review your decisions periodically to make sure they are still consistent with your goals. You should also consider any investments you may have outside the plan when making your investment choices. These target asset mixes were developed by Strategic Advisers, Inc., a registered investment advisor and Fidelity Investments company, based on the needs of a typical retirement plan participant.

## Diversify within each asset group

The same principle that applies to asset allocation applies to diversification within each asset group. Spreading assets among different types of stocks and bonds can help ensure that your portfolio is not exposed to the negative performance of any one type of investment.



Not all stocks or bonds perform identically. Within each asset class there are subgroups that typically have different risk and performance characteristics and that may complement each other, further helping to diversify your investment portfolio.

## Fixed-income

A well-diversified fixed-income portfolio should include securities from several categories of debt investments:

- **Short-, intermediate-, and long-term** maturity investment-grade bonds
- **High yield** bonds
- **Inflation-protected** bonds

Historically, these segments of the fixed-income market have performed relatively independently.

### FIXED-INCOME CYCLES:

Calendar year returns, 1998–2007

- **Short-Term Bonds** (LB 1–3 Year Government/Credit Index)
- **High Yield Bonds** (ML U.S. High Yield Master II Index)
- **Intermediate-Term Bonds** (Lehman Brothers U.S. Aggregate Index)
- **Floating Rate Bonds** (S&P/LSTA Leveraged Performing Loan Index)\*

|      | Best ← |       |       | → Worst |
|------|--------|-------|-------|---------|
| 1998 | 8.67%  | 6.99% | 5.25% | 2.94%   |
| 1999 | 3.65%  | 3.16% | 2.43% | -0.83%  |
| 2000 | 11.63% | 8.07% | 5.14% | -5.19%  |
| 2001 | 8.79%  | 8.42% | 4.48% | 3.34%   |
| 2002 | 10.27% | 6.29% | 2.63% | -0.53%  |
| 2003 | 27.97% | 9.78% | 4.11% | 2.82%   |
| 2004 | 10.87% | 5.29% | 4.34% | 1.28%   |
| 2005 | 5.28%  | 2.78% | 2.43% | 1.76%   |
| 2006 | 10.76% | 6.93% | 4.33% | 4.26%   |
| 2007 | 6.96%  | 6.83% | 2.53% | 1.99%   |

Source: FMR LLC.

**Past performance is no guarantee of future results.**

**It is not possible to invest directly in an index.**

**Index performance is not meant to represent that of any Fidelity mutual fund.**

Please see last page for index definitions.

\* Returns for 1998 and 1999 are of the CSFB Leveraged Loan Index.

## Domestic equities

A well-diversified domestic equity portfolio might contain stocks based on:

- **Company size**, i.e., its capitalization, or value in dollars.
- **Industry sector**, such as technology, utilities, consumer staples, media, real estate.
- **Earnings potential**, i.e., growth stocks, those of companies enjoying faster earnings growth; value stocks, those of companies that are undervalued in the market.

The following matrix shows the 10-year average performance of different types of domestic equities. You can see that there are excellent investing opportunities in each sector. Many investors overweight their portfolios with large-cap stocks, and by doing so, they may miss out on strong returns in other segments of the equities market.

### 10-YEAR AVERAGE ANNUAL PERFORMANCE

|       | Value                                 | Blend                           | Growth                                 |
|-------|---------------------------------------|---------------------------------|--|
| Large | Russell Top 200 Value<br><b>6.67%</b> | Russell Top 200<br><b>5.04%</b> | Russell Top 200 Growth<br><b>2.96%</b> |
| Mid   | Russell Midcap Value<br><b>10.18%</b> | Russell Midcap<br><b>9.91%</b>  | Russell Midcap Growth<br><b>7.59%</b>  |
| Small | Russell 2000 Value<br><b>9.06%</b>    | Russell 2000<br><b>7.08%</b>    | Russell 2000 Growth<br><b>4.32%</b>    |

Source: FMR LLC., as of 12/31/07.

## International equities

A well-diversified international portfolio might include stocks that differ in terms of:

- **Level of economic development**, e.g., developed economy vs. emerging market
- **Region of the world**, e.g., Asia, Europe, South America
- **Country** in which the stock-issuing company resides

The table below is a good illustration of the tremendous investment potential in the world's markets. It also illustrates why investors should not limit themselves to domestic U.S. stocks.

### WORLD PERFORMANCE

| Country        | Annualized returns |        |        |
|----------------|--------------------|--------|--------|
|                | 1-Yr               | 3-Yr   | 5-Yr   |
| Australia      | 15.20%             | 20.27% | 19.47% |
| Brazil         | 49.70%             | 39.85% | 42.99% |
| Canada         | 9.89%              | 17.28% | 18.24% |
| China          | 66.66%             | 54.00% | 47.40% |
| France         | 2.13%              | 15.87% | 14.82% |
| Germany        | 21.94%             | 23.40% | 22.52% |
| Hong Kong      | 41.57%             | 26.02% | 28.05% |
| India          | 54.16%             | 48.29% | 44.40% |
| Japan          | -10.21%            | 11.66% | 13.62% |
| Mexico         | 13.06%             | 32.31% | 37.19% |
| United Kingdom | 6.54%              | 13.58% | 14.18% |
| USA            | 5.44%              | 8.33%  | 12.45% |

Source: Ibbotson as of 12/31/07. Based on MSCI Country Indices.

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## Mutual fund solutions

As we mentioned at the outset, diversification is neither complicated nor difficult.

Implementing a diversification strategy may be accomplished in a couple of ways. You can, of course, build a well-diversified portfolio by researching and assembling individual securities. But there's a simpler, more efficient way to achieve a balanced investment mix – with mutual funds.

### Ready-made diversification

Mutual funds make it easy to apportion your investments among asset classes and asset subgroups. Each fund typically represents one specific asset segment. It might cover a wide range of equities, for instance, or an equity subgroup like small-cap stocks. Or it might specialize in a niche market such as technology or emerging markets debt.

Mutual funds with broad coverage of equities and fixed-income are often used as a core portfolio holding. Around this core you can add mutual funds that focus on specific segments within equities or fixed-income. In this way individual mutual funds may be combined to achieve a breadth and level of diversification to suit any investor's financial goals, time horizon, and appetite for risk.

## Asset allocation funds

An increasing number of mutual funds now also offer built-in asset allocation. They preset a certain percentage mix of stocks and bonds with a choice of typically three allocation strategies: conservative, moderate, and aggressive. These balanced or “lifestyle” funds offer the investor a convenient core asset allocation based on his or her risk tolerance.

## Lifecycle funds

Lifecycle, or target-date, funds are funds of funds. They combine portions of several mutual funds to create a desired asset allocation and investment mix. Lifecycle funds are designed for specific time-targeted long-range savings goals like retirement, where the asset allocation strategy needs to become more conservative as a target date approaches.

These funds utilize active management and constant monitoring to adjust the asset allocation periodically and maintain the risk/return balance best suited to the individual’s target date.





## Your advisor can help

Like many investors, you probably agree that diversification makes good sense. Yet when it comes to actually following through, you may hang back and keep putting it off.

There are a number of reasons why investors delay diversifying: you may think you don't have a large enough portfolio to make it worthwhile, or that diversification is too complicated, or that bonds will crimp your returns, or that stocks are too risky. Or you might simply feel a low level of uncertainty.

This is the time when a financial advisor can make all the difference by helping you:

- Map out your time horizon
- Define your financial goals
- Understand your risk tolerance
- Create a realistic balance of investments
- Monitor your portfolio over time and reallocate assets as needed

Even more valuable may be your advisor's skill and influence in helping make sure you stay focused on your goals, stay invested, and stay diversified so that you may enjoy better returns with less risk and less stress over time.

**Credit Suisse First Boston (CSFB) Leveraged Loan Index** is a market value-weighted index designed to represent the investable universe of the U.S. dollar-denominated leveraged loan market. This index includes reinvested dividends and capital gains, if any, and excludes the effects of a sales charge.

**Lehman Brothers U.S. Aggregate Index** is a market value-weighted index of investment-grade fixed-rate debt issues, including government, corporate, asset-backed, and mortgage securities, with maturities of one year or more.

**Lehman Brothers 1–3 Year Government/Credit Bond Index** is a market value-weighted index of government and investment-grade corporate fixed-rate debt issues with maturities between 1 and 3 years.

**Merrill Lynch High Yield Master II Index** is a market value-weighted index of all domestic and Yankee high yield bonds, including deferred interest bonds and payment-in-kind securities. Issues included in the index have maturities of one year or more and have a credit rating lower than BBB-/Baa3 but are not in default.

**Morgan Stanley Capital International (MSCI) individual country indices** are free float-adjusted market capitalization indices that are designed to measure equity market performance in each individual country.

**Morgan Stanley Capital International (MSCI) EAFE Index** is an unmanaged market capitalization-weighted index that is designed to represent the performance of developed stock markets outside the United States and Canada.

**Russell 2000® Index** is a market capitalization-weighted index of the stocks of the 2,000 smallest companies included in the 3,000 largest U.S.-domiciled companies.

**Russell 2000 Growth Index** is a market capitalization-weighted index of those stocks of the 2,000 largest U.S.-domiciled companies that exhibit growth-oriented characteristics.

**Russell 2000 Value Index** is a market capitalization-weighted index of those stocks of the 2,000 largest U.S.-domiciled companies that exhibit value-oriented characteristics.

**Russell Midcap® Index** measures the performance of the 800 smallest companies in the Russell 1000 Index, which represent approximately 25% of the total market capitalization of the Russell 1000 Index.

**Russell Midcap Growth Index** measures the performance of those Russell Midcap companies with higher price-to-book ratios and higher forecasted growth values. The stocks are also members of the Russell 1000 Growth Index.

**Russell Midcap Value Index** measures the performance of those Russell Midcap companies with lower price-to-book ratios and lower forecasted growth values. The stocks are also members of the Russell 1000 Value Index.

**Russell Top 200® Index** measures the performance of the 200 largest companies in the Russell 1000 Index, which represents approximately 75% of the total market capitalization of the Russell 1000 Index.

**Russell Top 200 Growth Index** measures the performance of those Russell Top 200 companies with higher price-to-book ratios and higher forecasted growth values. The stocks are also members of the Russell 1000 Growth Index.

**Russell Top 200 Value Index** measures the performance of those Russell Top 200 companies with lower price-to-book ratios and lower forecasted growth values. The stocks are also members of the Russell 1000 Value Index.

**S&P 500** is an unmanaged market capitalization-weighted index of common stock prices of 500 widely held U.S. stocks and includes reinvestment of dividends.

**S&P/LSTA Leveraged Performing Loan Index** is a market value-weighted index designed to represent the performance of U.S. dollar-denominated institutional leveraged performing loan portfolios (excluding loans in payment default) using current market weightings, spreads, and interest payments.

All indices are unmanaged and include reinvestment of dividends and interest income.

Your Advisor  
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