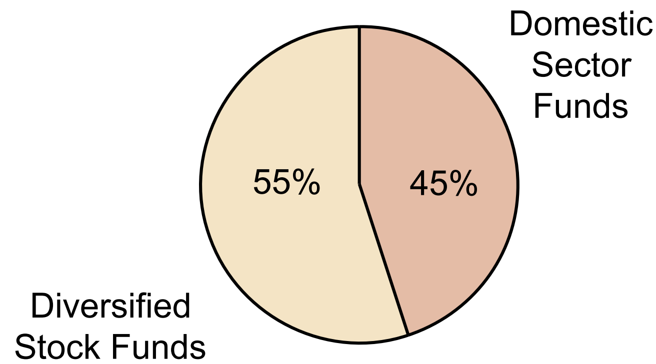
Medium Risk Portfolio

Number of funds held: 7-10
Relative Volatility: 0.8 to 1.2



The Medium Risk Portfolio seeks long-term growth by investing approximately 45% of assets in domestic sector funds (typically Fidelity Select Portfolios), and 55% in diversified stock funds. Usually it will hold six different sector funds and two or three diversified stock funds. The diversified stock fund holdings are normally domestic growth funds from Fidelity's lineup, but if foreign valuations are attractive the portfolio may invest in an international fund – usually for 5-15% of the total portfolio.

The domestic sector portion of the portfolio attempts to invest in industry groups that are in the process of being recognized for their long-term potential. Such sectors are identified through the use of a volatility model that evaluates the standard deviation of monthly gains and losses over a period of up to 36 months, while comparing each sector's result with a baseline period of up to10 years. Each industry group is ranked against all other non-gold sectors in the Fidelity lineup. Normally, six sectors are held from the upper quartile of the resulting ranking. Together, these funds account for roughly 200 unique stock positions, but there can be significant overlap between sectors. In addition, many of the sector funds are heavily concentrated, with their top 10 holdings accounting for more than 50% of assets.

The diversified portion of the portfolio attempts to invest in attractively positioned non-sector stock funds, both domestic and foreign. Factors considered include historical performance, overall volatility, stylebox position, industry mix, cash level, foreign weighting, expense ratio, and manager history. An effort is also made to pick diversified funds that complement the sector side of the portfolio, with a goal of reducing overall volatility. In the future, we may evaluate stock funds from the standpoint of active share and tracking error. This assessment provides insight into how the manager is positioning the portfolio. Studies have shown that funds with high active share and low tracking error tend to outperform their peers.

Typically, the Medium Risk Portfolio holds the equivalent of 300-400 unique stock positions, and is fully invested in stock funds. It competes with the S&P 500 index. It focuses heavily on Fidelity's retail mutual funds because we believe this provides improved risk-adjusted performance relative to competing alternatives, but may invest in non-Fidelity funds if we believe improved risk-adjusted performance is available for a particular objective. The portfolio typically holds actively managed funds, but may invest in index funds during periods of uncertainty or when we believe large-cap stocks will lead the market. Alternative holdings, such as high-yield bond funds or real estate funds, may be used for a portion of the portfolio if valuations are deemed compelling.

During bearish market conditions the portfolio may become more defensive, but money market funds and investment-grade bond funds are not usually held. ■