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Fidelity
Management &
Research Company

Insights into Fixed Income

Fixed Income Market and Portfolio Review

In 2007, most of Fidelity's taxable bond funds experienced a very challenging year, producing total returns that significantly lagged their respective investment benchmarks. Major detractors from performance include the relatively weak results of all non-Treasury sectors of the investment grade bond market and the particularly poor performance of subprime mortgage securities. Fidelity taxable bond funds generally held overweight positions in a number of these sectors, including corporate, asset-backed, commercial mortgage backed, and subprime mortgages.

In contrast to many Fidelity taxable bond funds, Fidelity municipal bond and most Fidelity government bond funds performed well in 2007. All Fidelity municipal bond funds beat their Lipper category averages in 2007.[1]

Bond Market Review

The bond market was uncharacteristically turbulent in 2007. Many investment-grade bond sectors suffered their worst relative performance on record compared to U.S. Treasuries. Even highly rated securities were not spared during this period with AAA-rated investments suffering materially.

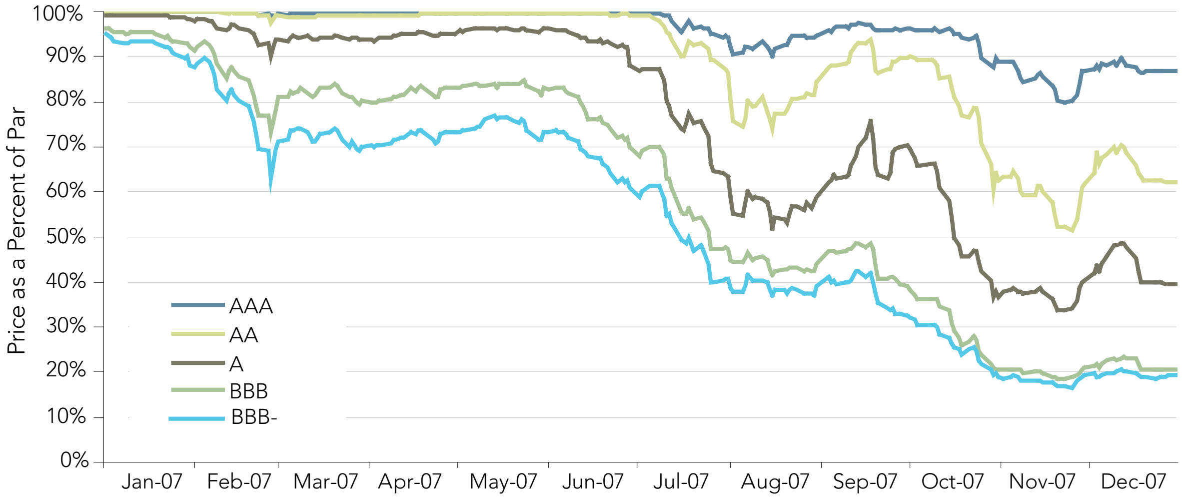
This unprecedented market volatility originated in the subprime residential mortgage sector. Subprime mortgage securities are bonds that are backed by pools of home loans that are issued to buyers with lower credit standing. These loans are then packaged and resold to institutional investors such as mutual funds. Prices of subprime mortgage securities fell when US home prices fell, when mortgage foreclosure rates rose, and when many traditionally large holders of these bonds, such as collateralized debt obligation (CDO) issuers and other leveraged investors, were forced to sell in order to meet redemption demands. Even highly rated subprime mortgage securities, which benefit from greater levels of credit support than lower rated securities, depreciated substantially. Exhibit 1, next page shows the price fall in the various rating tiers of 2006 version 2 of the ABX.HE index, which represents a standardized basket of these bonds. The index has been used as a proxy for the performance of 2006-originated subprime mortgage securities.

Portfolio Review and Outlook

Relative weakness in all non-Treasury sectors resulted in significant underperformance for most Fidelity taxable bond funds. The funds held overweight positions in a number of these sectors, including corporate, asset-backed and commercial–mortgage backed issues, with sub-prime residential mortgage investments representing the largest detractor from performance. Although the majority of the funds' subprime mortgage investments were in the highest rated AAA and AA layers of the capital structure, large price declines for even the strongest securities in this sector resulted in significant overall fund underperformance.

[1] Lipper Inc. is a nationally recognized organization that ranks the performance of mutual funds. Lipper Category Averages are averages of the performance of all mutual funds within their respective investment classification category.

EXHIBIT 1: Steep decline in the price of subprime mortgage securities (ABX.HE Indices)



Source: MarkIt Group Limited, FMR as of 12/31/2007

While we expect the subprime sector to experience further turbulence in 2008, we believe that most AAA and AA rated subprime mortgage holdings will ultimately pay full principal and interest to bondholders. At the same time, we believe that some single A and BBB-rated subprime securities remain at risk of principal loss. Fidelity's research employs what we had believed to be conservative economic assumptions in forecasting the future performance of the subprime sector. Fidelity has re-evaluated every subprime mortgage security in the portfolios with a focus on rigorously stress-testing both fundamental collateral quality and structural integrity. While a small number of securities were identified as sale candidates, we re-affirmed the creditworthiness of the vast majority of our subprime holdings.

Other securitized investments, primarily concentrated in AAA-rated residential mortgage, commercial mortgage, and asset backed sectors, also detracted from investment performance. While we have generally been underweight agency-backed pass-through mortgages, portfolios are overweight agency hybrid securities and highly rated collateralized mortgage obligations. Commercial mortgage-backed exposure is focused on AAA-rated super senior bonds whose credit quality benefits from a very high level of structural protection. We have added investments in this sector as valuations have fallen to historic levels. In addition, our overweight to the corporate bond

EXHIBIT 2: Subprime mortgage security exposure of some Fidelity bond funds

Fidelity Fund	Subprime Mortgage Bond Exposure (12/31/2007)
Fidelity & FA Ultra Short Bond	19%
Fidelity & FA Mortgage Securities	8%
Fidelity Short-Term Bond	6%
FA Short Fixed Income	6%
Fidelity & FA Investment Grade Bond	5%
FA Intermediate Bond	4%
Fidelity Intermediate Bond	4%
Fidelity & FA Total Bond	3%
Fidelity U.S. Bond Index	3%
Fidelity & FA Inflation-Protected Bond	2%

Source: FMRCo

sectors also negatively impacted investment returns during the period.

While we expect volatility in the bond market to persist in 2008, we believe that historically attractive valuations and supportive fundamental conditions across much of the corporate and securitized markets will provide significant opportunities to add value in the portfolios.

We are disappointed with the performance of some of our taxable bond funds in 2007. These results have broken the track record of strong performance relative to what our competitors achieved during the past decade. This success was built on a broad and deep research capability and investment discipline that stressed in-depth credit analysis and an assessment of the risks associated with each investment. While we hold steadfast to our investment discipline, the experiences we gained from the subprime crisis will serve to strengthen our research process and we believe our shareholders will benefit from this going forward.

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Fidelity Distributors Corporation, 82 Devonshire Street, Boston, MA 02109

Fidelity Brokerage Services, Member NYSE/SIPC, 100 Summer Street, Boston, MA 02110