MUTUAL FUND Investor Guide

THE Investor Guide TO FIDELITY FUNDS

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Matthew Sauer is the Founder and Chief Investment Officer of the Mutual Fund Investor Guide family of newsletters. Each month he analyzes and provides buy, sell and hold recommendations for hundreds of mutual funds and ETFs in the Investor Guide to Fidelity Funds, Investor Guide to Vanguard Funds, as well as the ETF Investor Guide.

Prior to founding the Mutual Fund Investor Guide, Matt was the President and Chief Investment Officer of the Fidelity Independent Adviser, ETF Report, and Sector Momentum Tracker.

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SPECIAL REPORT: The Best Fidelity Fund to Buy Before 2015

FIDELITY FLOATING RATE HIGH INCOME FUND (FFRHX)

With the risk of higher interest rates becoming reality in 2015, investors looking for high income face a tough set of choices. Until now, holding long-dated Treasury and investment grade bonds has been a good way to earn higher income, but rising interest rates will lead to capital losses on funds holding these securities. High-yield bond funds mitigate some of this risk, but they too are susceptible to rising rate. Another option is to use floating-rate securities that reset their interest rates based on changes in the market. These funds pay a lower yield than you can currently obtain in the market, but if rates rise, these bonds will decline much less, while the income of the fund will rise.

Fidelity is a mutual fund industry giant that has funds covered many asset categories. One of its brightest spots has been its fixed-income operations. Fidelity offers one of the best no-load choices in the floating-rate category, which can be a hedge against rising interest rates. Established on August 16, 2000, The Fidelity Floating Rate High Income Fund (FFRHX) is a mutual fund that seeks a high level of current income, while mitigating the risk from rising interest rates.

Listed by Morningstar in the Bank Loan category, the fund has over $15 billion under management. The fund invests at least 80 percent of net assets under management in floating rate loans, which are typically lower-quality debt instruments, as well as other floating rate debt securities. The debt issuers are usually companies with lower credit ratings. The floating-rate securities are senior in the issuing firm's capital structure and are typically secured by corporate assets. They also reset their interest rates every 30 to 90 days to a point slightly above the current short-term benchmark. The fund also purchases investment-grade debt, money market securities and repurchase agreements. Fund managers use fundamental analysis of each domestic and foreign issuer's industry position and financial condition as well as overall market and economic circumstances to select investments.

The fund has been under the direction of Eric Mollenhauer since April 1, 2013. He has more than two decades of experience in the bank loan and high-yield investment markets. FFRHX is suitable for retirement accounts, including simple IRAs. The fund's fiscal year ends in October.

INVESTMENT STRATEGY

Prior to Mr. Mollenhauer assuming the helm of the fund in 2013, FFRHX was one of the most conservative funds in the bank loan category. Christine McConnell, the former manager, concentrated on higher quality securities and has at various times held a significant portion of the total portfolio in cash. Ms. McConnell favored debt instruments at the higher-quality end of the below-investment grade market issued by larger, more liquid entities. The cash position was also used to manage liquidity. This strategy served investors well during the financial crisis of 2008 when the fund was down 16.5 percent compared to the category average of 30 percent. The conservative approach that served the fund well in the down market caused the fund to trail the vast majority of its peers during the risk-led markets of the ensuing years. The improving U.S. economy created an environment in which lower rated speculative loans have generally outperformed the fund and the category as a whole. The fund's conservative approach has hampered its relative returns.

While new manager Mollenhauer signaled that he planned to be more opportunistic than his predecessor, this strategy has yet to unfold as the market has provided few opportunities to put the plan into effect. Bank loans have been trading at or near par with low default rates. As a result, the overall credit quality profile of the fund has changed very little. The fund has approximately half of its assets in BB and BBB rated securities with a mix of 41 and 7 percent respectively. The fund has decreased its investment in CCC or lower rated debt securities to 3 percent, which is approximately half its normal position while increasing its allocation of B rated securities to 39 percent. Where Mollenhauer has made a strong impact is his decision to reduce the cash holdings from 11 percent to 5 percent in April 2013. Another indicator of a more aggressive stance in the fund's philosophy is the investment in Caesars, a troubled casino name. Mollenhauer deflects criticism of the decision by saying that he believes the location of the debt instrument in the company's financial structure offers investors sufficient protection.

Although the fund still lags its peers, Mollenhauer has not increased investments in riskier assets despite his more aggressive stance while managing the Fidelity Series Floating Rate High Income Fund (FFHCX). Mollenhauer's strategy of occasionally investing cash in more aggressive instruments should produce higher returns in a healthier market. While the fund may become more aggressive and relinquish a portion of its historic downside protection, it is unlikely that FFRHX will be significantly riskier investment in the future. The fund should remain one of the more cautious investment offerings in the bank loan category. Aligning his own interests with those of his shareholders, Mollenhauer has $1 million invested in the fund's portfolio.

Security selection follows a bottom-up approach emphasizing positions recommended by Fidelity's analytical research team. Investments are scrutinized based on the loan's collateral coverage and the issuing firm's financial stability and cash flow.

HOLDINGS

As of September 30, 2014, FFRHX held 88.85 percent of its assets in term and revolving loans. The remainder of assets under management was invested in other floating rate instruments, fixed rate corporate bonds and cash with a distribution of 2.48, 3.96 and 4.71 percent, respectively. The regional diversification of the fund is 90.6 percent domestic holdings and 9.4 percent foreign. Companies based in Australia, The Netherlands and Israel issued the largest percentage of foreign holdings. FFRHX portfolio holdings compare to the bank loan category that has an average loan portfolio of 43.11 percent with corporate bonds, securitized debt instruments and cash or cash equivalent of 18.85, 0.6 and 36.8 percent, respectively.

The top 10 holdings comprise 15.86 percent of the fund's assets. The companies involved include Heinz, Community Health, HCA Term A., Hilton Worldwide and Fortescue Metals Group as well as Caesars Properties, Dell, Altice Financial, BMC Software and HCA Term B. The fund is overweight telecommunications, energy, lodging/casinos, cable/satellite television and utilities while being underweight chemicals/plastics, automotive, super retail, publishing/printing and business equipment/services.

HISTORICAL PERFORMANCE

With a portfolio of bonds, loans and other debt instruments, FFRHX, like its peers, is designed to generate the best returns in a strong and improving economy. It can suffer in a down market or other periods where investor appetite for riskier assets wanes. The fund has generated returns of 2.82 percent, 5.03 percent, 4.77 percent, 4.36 percent and 4.35 percent on an annualized basis for the previous 1-, 3- 5-, 10-year periods and the life of the fund, respectively. These returns can be compared to the equivalent returns for the underlying S&P/LSTA Leveraged Performing Loan Index of 3.9 percent, 6.73 percent, 6.47 percent, 5.21 percent and 5.15 percent.

The Bank Loan category for these same periods showed a return of 3.15 percent, 6.25 percent, 5.93 percent and 3.75 percent. The inception period return is N/A due to the category being created after FFRHX was established.

These returns produce a Morningstar rank of 65, 91, 89 and 15 for the previous 1-, 3-, 5-, 10-year periods. Morningstar ratings show FFRHX delivering below average returns for the most recent 3- and 5-year periods, as expected given the conservative approach that was kept after 2008, with above average returns for the last 10 years and average returns since the fund's inception. Lipper has the fund ranked as number 111 out of 190 funds for the past year as well as number 82 out of 91 and 6th out of 39 for the most recent 5- and-10-year periods.

INCOME

The fund pays a monthly income distribution. The fund currently yields 3.63 percent.

PURCHASING AND FEES

The minimum initial investment in FFRHX for IRA and taxable accounts is $2,500. There are no restrictions on subsequent investments. The fund requires a minimum maintenance balance of $2,000. While the fund does not have a check-writing feature, it does support direct deposits and automatic account builder functions.

In addition to an expense ratio of 0.70 percent, FFRHX has a short-term redemption fee of 1.0 percent and a short-term redemption period of 60 days. There are a maximum number of exchange redemptions as well. The fund does not have any 12b-1 fees.

RISK AND VOLATILITY MEASUREMENTS

Morningstar rates FFRHX risk level as average among the Bank Loan category. Fixed income securities face interest rate risks as the face value of the bonds will decline as rates increase, however this risk is mitigated by holding floating rate securities that can increase their yield.

FFRHX has a turnover rate of 60 percent.

The Beta for FFRHX is 0.25. This measure of volatility shows how much the fund's historical returns deviate from an underlying benchmark of the S&P/LSTA Leveraged Performing Loan Index. The Index is market value-weighted and designed to replicate the returns of institutional leveraged U.S. dollar-denominated loan portfolio utilizing current interest rates, spreads and market weightings. The Beta for Fidelity's Total Bond Fund and the Bank Loan category are 1.07 and 0.53, respectively. A rating of 1.0 shows no deviation from the benchmark index. Since interest rates are one of major factors affecting bond prices, the effect of floating rate securities is visible in the much lower beta.

The Sharpe ratio is a measure of adjusted historical performance determined by dividing the fund's excess returns by the return's standard deviation. This gives a risk adjusted measurement of the fund' returns. FFRHX has a Sharpe ratio of 1.98 based on a standard deviation of 2.46, which compares to the equivalent ratings for the bank loan category of 2.59 and 2.45. The ratings for the Total Bond Fund are 1.27 and 2.97, respectively. Morningstar has assigned an average risk rating to FFRHX for the previous 3-year period as well as a below average and low rating for the 5- and 10-year periods. The risk rating since fund inception is below average.

RECOMMENDATION

The fund's comparatively lower risk and low expense ratio as well as four-out-of-five star and Bronze Analyst ratings by Morningstar support a buy recommendation. The fund's overall rating is based on a weighted average of the fund's 3-, 5- and 10-year performance figures associated with the applicable Morningstar Metrics.

Runner Ups

The Spartan Intermediate Treasury Bond Index (FIBIX) seeks a high level of current income by investing at least 80 percent of net assets in securities found in the Barclay's U.S. 5 to 10 Year Treasury Bond Index. The fund maintains an average dollar-weighted maturity between 3 and 10 years. FIBIX managers attempt to replicate the returns of the underlying benchmark index with fewer holdings by using a statistical sampling technique based on factors such as the securities maturity, duration, structure, interest rate sensitivity and credit quality. The funds average maturity makes it vulnerable to a rising interest rate environment.

Seeking to generate a high level of current income, the non-diversified Fidelity Global Bond Fund (FGBFX) invests in various securities from around the world including those from issuers located in emerging markets. At least 80 percent of net assets are allocated to investment-grade debt securities of all types and their equivalent repurchase agreement. The remaining 20 percent of assets can be invested in lower quality debt instruments. The global aspect of the fund increases its currency risk if there is an extended rally in the U.S. dollar.

Pursuant to its goal of generating a high level of current income, the Fidelity Corporate Bond Fund (FCBFX) invests 80 percent of net assets in investment-grade corporate bonds and other debt instruments as well as their associated repurchase agreements issued by domestic and foreign companies. The fund attempts to replicate the risks and returns of the Barclay's U.S. Credit Bond Index. The remaining 20 percent may be invested in lower quality debt securities. The average maturity of the fund's holdings makes it sensitive to rising interest rates.

If you have any questions or comments about these funds, we would be delighted to speak with you. Please call us at (888) 252-5372, Monday through Friday 8:30am to 5:30pm, eastern time. You can also email me at Matt@mutualfundinvestorguide.com.

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THE FIDELITY FLOATING RATE HIGH INCOME FUND (FFRHX) TOP TEN HOLDINGS

Company Name	% of Assets	% Coupon
Heinz Term B-2 6/7/2020	2.5	3.50
Community Health Trm D 1/27/21	2.09	4.25
Hca Inc Term A-4 02/02/16	1.82	2.69
Fortescue Mtls Grp Term B 6/19	1.73	4.25
Hilton Worldwid Trm B 10/25/20	1.72	4.00
Caesars Prop Tm B 1In 10/11/20	1.68	7.00
Dell Term B 04/29/20	1.24	4.50
Altice Financing Trm B 6/24/19	1.02	5.50
Hca Term B-5 03/31/17	0.97	3.03
Bmc Software Us Term B 9/10/20	0.93	5.00

FUND CHARACTERISTICS

YTD Return	1.23%
1 Year Average Annual Return	2.82%
3 Year Average Annual Return	5.03%
5 Year Average Annual Return	4.77%
10 Year Average Annual Return	4.36%
Since Inception Average Annual Return	4.35%
Morningstar Category	Bank Loan
SEC Yield	3.40%
Turnover	60.00%
NAV	9.84
Net Assets	15.02 B
Morningstar Overall Rating	4 Star
Morningstar Risk Rating	2
Investment Minimum	$2,500
Front / Deffered Load	None
Short - Term Redemption Period / Fee	60 days / 1.00%
Expense Ratio	0.70%
Holdings	435

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