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VANGUARD EXPLORER FUND INC

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PART B

VANGUARD EXPLORER FUND, INC.

STATEMENT OF ADDITIONAL INFORMATION

FEBRUARY 10, 1995; REVISED FEBRUARY 22, 1995

This Statement is not a prospectus but should be read in conjunction with the Fund's current Prospectus (dated February 10, 1995). To obtain the Prospectus please call the Investor Information Department:

1-800-662-7447

TABLE OF CONTENTS

<TABLE>
<CAPTION>

	PAGE

<S>	<C>
Investment Objective and Policies.....	1
Purchase of Shares.....	5
Redemption of Shares.....	5
Dividends and Capital Gains Distributions.....	5
Yield and Total Return.....	6
Investment Limitations.....	6
Management of the Fund.....	8
Investment Advisory Services.....	10
Portfolio Transactions.....	15
General Information About the Fund.....	15
Performance Measures.....	16
Financial Statements.....	17

</TABLE>

INVESTMENT OBJECTIVE AND POLICIES

The following policies supplement the Fund's investment objective and policies set forth in the Prospectus.

REPURCHASE AGREEMENTS The Fund may invest in repurchase agreements with commercial banks, brokers or dealers either for defensive purposes due to market conditions or to generate income from its excess cash balances. A repurchase agreement is an agreement under which the Fund acquires a money market instrument (generally a security issued by the U.S. Government or an agency thereof, a banker's acceptance or a certificate of deposit) from a commercial bank, broker or dealer, subject to resale to the seller at an agreed upon price and date (normally, the next business day). A repurchase agreement may be considered a loan collateralized by securities. The resale price reflects an agreed upon interest rate effective for the period the instrument is held by the Fund and is unrelated to the interest rate on the underlying instrument. In these transactions, the securities acquired by the Fund (including accrued interest earned thereon) must have a total value in excess of the value of the repurchase agreement and are held by the Fund's custodian bank until repurchased. In addition, the Fund's Board of Directors will monitor the Fund's repurchase agreement transactions generally and will establish guidelines and standards for review by the investment adviser of the creditworthiness of any bank, broker or dealer party to a repurchase agreement with the Fund. No more than an aggregate of 15% of the Fund's assets, at the time of investment, will be invested in repurchase agreements having maturities longer than seven days and securities subject to legal or contractual restrictions on resale, or for which there are no readily available market quotations.

The use of repurchase agreements involves certain risks. For example, if the other party to the agreement defaults on its obligation to repurchase the underlying security at a time when the value of the security has declined, the Fund may incur a loss upon disposition of the security. If the other party to the agreement becomes insolvent and subject to liquidation or reorganization under the Bankruptcy Code or other laws, a court may determine that the

underlying security is collateral for a loan by the Fund not within the control of the Fund and therefore the realization by the Fund on such collateral may be automatically stayed. Finally, it is possible that the Fund may not be able to substantiate its interest in the underlying security and may be

1

2

deemed an unsecured creditor of the other party to the agreement. While the Fund's management acknowledges these risks, it is expected that they can be controlled through careful monitoring procedures.

LENDING OF SECURITIES The Fund may lend its portfolio securities to qualified institutional investors who need to borrow securities in order to complete certain transactions, such as covering short sales, avoiding failures to deliver securities, or completing arbitrage operations. By lending its portfolio securities, the Fund attempts to increase its income through the receipt of interest on the loan. Any gain or loss in the market price of the securities loaned that might occur during the term of the loan would be for the account of the Fund. The Fund may lend its portfolio securities to qualified brokers, dealers, banks or other financial institutions, so long as the terms and the structure of such loans are not inconsistent with the Investment Company Act of 1940, or the Rules and Regulations or interpretations of the Securities and Exchange Commission thereunder, which currently require that (a) the borrower pledges and maintains with the Fund collateral consisting of cash, a letter of credit, or securities issued or guaranteed by the United States Government having a value at all times not less than 100% of the value of the securities loaned, (b) the borrower adds to such collateral whenever the price of the securities loaned rises (i.e., the borrower "marks to the market" on a daily basis), (c) the loan is made subject to termination by the Fund at any time, and (d) the Fund receives reasonable interest on the loan (which may include the Fund's investing any cash collateral in interest bearing short-term investments), any distributions on the loaned securities and any increase in their market value. The Fund will not lend portfolio securities if, as a result, the aggregate of such loans exceeds 33 1/3% of the Fund's total assets. Loan arrangements made by the Fund will comply with all other applicable regulatory requirements, including the rules of the New York Stock Exchange, which rules presently require the borrower, after notice, to redeliver the securities within the normal settlement time of five business days. All relevant facts and circumstances, including the creditworthiness of the broker, dealer or institution, will be considered in making decisions with respect to the lending of securities, subject to review by the Fund's Board of Directors.

At the present time, the Staff of the Commission does not object if an investment company pays reasonable negotiated fees in connection with loaned securities, so long as such fees are set forth in a written contract and approved by the investment company's directors (trustees). In addition, voting rights may pass with the loaned securities, but if a material event will occur affecting an investment on loan, the loan must be called and the securities voted.

FUTURES CONTRACTS AND OPTIONS The Fund may enter into futures contracts, options, and options on futures contracts for several reasons: to maintain cash reserves while simulating full investment, to facilitate trading, to reduce transaction costs, or to seek higher investment returns when a futures contract is priced more attractively than the underlying equity security or index. Futures contracts provide for the future sale by one party and purchase by another party of a specified amount of a specific security at a specified future time and at a specified price. Futures contracts which are standardized as to maturity date and underlying financial instrument are traded on national futures exchanges. Futures exchanges and trading are regulated under the Commodity Exchange Act by the Commodity Futures Trading Commission ("CFTC"), a U.S. Government agency.

Although futures contracts by their terms call for actual delivery or acceptance of the underlying securities, in most cases the contracts are closed out before the settlement date without the making or taking of delivery. Closing out an open futures position is done by taking an opposite position ("buying" a contract which has previously been "sold" or "selling" a contract previously "purchased") in an identical contract to terminate the position. Brokerage commissions are incurred when a futures contract is bought or sold.

Futures traders are required to make a good faith margin deposit in cash or government securities with a broker or custodian to initiate and maintain open positions in futures contracts. A margin deposit is intended to assure completion of the contract (delivery or acceptance of the underlying security)

if it is not terminated prior to the specified delivery date. Minimal initial margin requirements are established by the futures exchange and may be changed. Brokers may establish deposit requirements which are higher than the exchange minimums. Futures contracts are customarily purchased and sold on margin that may range upward from less than 5% of the value of the contract being traded.

After a futures contract position is opened, the value of the contract is marked to market daily. If the futures contract price changes to the extent that the margin on deposit does not satisfy margin requirements,

2

3

payment of additional "variation" margin will be required. Conversely, change in the contract value may reduce the required margin, resulting in a repayment of excess margin to the contract holder. Variation margin payments are made to and from the futures broker for as long as the contract remains open. The Fund expects to earn interest income on its margin deposits.

Traders in futures contracts may be broadly classified as either "hedgers" or "speculators." Hedgers use the futures markets primarily to offset unfavorable changes in the value of securities otherwise held for investment purposes or expected to be acquired by them. Speculators are less inclined to own the securities underlying the futures contracts which they trade, and use futures contracts with the expectation of realizing profits from fluctuations in the underlying securities. The Fund intends to use futures contracts only for bonafide hedging purposes.

Regulations of the CFTC applicable to the Fund require that all of its futures transactions constitute bonafide hedging transactions. The Fund will only sell futures contracts to protect securities it owns against price declines or purchase contracts to protect against an increase in the price of securities it intends to purchase. As evidence of this hedging interest, the Fund expects that approximately 75% of its futures contract purchases will be "completed;" that is, equivalent amounts of related securities will have been purchased or are being purchased by the Fund upon sale of open futures contracts.

Although techniques other than the sale and purchase of futures contracts could be used to control the Fund's exposure of market fluctuations, the use of futures contracts may be a more effective means of hedging this exposure. While the Fund will incur commission expenses in both opening and closing out futures positions, these costs are lower than transaction costs incurred in the purchase and sale of the underlying securities.

RESTRICTIONS ON THE USE OF FUTURES CONTRACTS The Fund will not enter into futures contract transactions to the extent that, immediately thereafter, the sum of its initial margin deposits on open contracts exceeds 5% of the market value of the Fund's total assets. In addition, the Fund will not enter into futures contracts to the extent that its outstanding obligations to purchase securities under these contracts would exceed 20% of the Fund's total assets.

RISK FACTORS IN FUTURES TRANSACTIONS Positions in futures contracts may be closed out only on an Exchange which provides a secondary market for such futures. However, there can be no assurance that a liquid secondary market will exist for any particular futures contract at any specific time. Thus, it may not be possible to close a futures position. In the event of adverse price movements, the Fund would continue to be required to make daily cash payments to maintain its required margin. In such situations, if the Fund has insufficient cash, it may have to sell portfolio securities to meet daily margin requirements at a time when it may be disadvantageous to do so. In addition, the Fund may be required to make delivery of the instruments underlying futures contracts it holds. The inability to close options and futures positions also could have an adverse impact on the ability of the Fund to hedge its portfolio effectively. The Fund will minimize the risk that it will be unable to close out a futures contract by only entering into futures which are traded on national futures exchanges and for which there appears to be a liquid secondary market.

The risk of loss in trading futures contracts in some strategies can be substantial, due to both the low margin deposits required and the extremely high degree of leverage involved in futures pricing. As a result, a relatively small price movement in a futures contract may result in immediate and substantial loss (as well as gain) to the investor. For example, if at the time of purchase, 10% of the value of the futures contract is deposited as margin, a subsequent 10% decrease in the value of the futures contract would result in a total loss of the margin deposit, before any deduction for the transaction costs, if the account were then closed out. A 15% decrease would result in a loss equal to

150% of the original margin deposit if the contract were closed out. Thus, a purchase or sale of a futures contract may result in losses in excess of the amount invested in the contract. The Fund also bears the risk that the Advisers will incorrectly predict future market trends. However, because the futures strategies of the Fund are engaged in only for hedging purposes, the Fund will not be subject to the risks of loss frequently associated with futures transactions. The Fund would presumably have sustained comparable losses if, instead of the futures contract, it had invested in the underlying financial instrument and sold it after the decline.

3

4

Utilization of futures transactions by the Fund does involve the risk of imperfect or no correlation where the securities underlying futures contracts have different maturities than the portfolio securities being hedged. It is also possible that the Fund could both lose money on futures contracts and also experience a decline in value of its portfolio securities. There is also the risk of loss by the Fund of margin deposits in the event of bankruptcy of a broker with whom the Fund has an open position in a futures contract or related option.

Most futures exchanges limit the amount of fluctuation permitted in futures contract prices during a single trading day. The daily limit establishes the maximum amount that the price of a futures contract may vary either up or down from the previous day's settlement price at the end of a trading session. Once the daily limit has been reached in a particular type of contract, no trades may be made on that day at a price beyond that limit. The daily limit governs only price movement during a particular trading day and therefore does not limit potential losses, because the limit may prevent the liquidation of unfavorable positions. Futures contract prices have occasionally moved to the daily limit for several consecutive trading days with little or no trading, thereby preventing prompt liquidation of future positions and subjecting some futures traders to substantial losses.

FEDERAL TAX TREATMENT OF FUTURES CONTRACTS The Fund is required for federal income tax purposes to recognize as income for each taxable year its net unrealized gains and losses on futures contracts held as of the end of the year as well as those actually realized during the year. In most cases, any gain or loss recognized with respect to a futures contract is considered to be 60% long-term capital gain or loss and 40% short-term capital gain or loss, without regard to the holding period of the contract. Furthermore, sales of futures contracts which are intended to hedge against a change in the value of securities held by the Fund may affect the holding period of such securities and, consequently, the nature of the gain or loss on such securities upon disposition. The Fund may be required to defer the recognition of losses on futures contracts to the extent of any unrecognized gains on related positions held by the Fund.

In order for the Fund to continue to qualify for federal income tax treatment as a regulated investment company, at least 90% of its gross income for a taxable year must be derived from qualifying income; i.e., dividends, interest, income derived from loans of securities, gains from the sale of securities and other income derived with respect to its business of investing in securities. In addition, gains realized on the sale or other disposition of securities held for less than three months must be limited to less than 30% of the Fund's annual gross income. It is anticipated that any net gain realized from the closing out of futures contracts will be considered gain from the sale of securities and therefore be qualifying income for purposes of the 90% requirement. In order to avoid realizing excessive gains on securities held less than three months, the Fund may be required to defer the closing out of futures contracts beyond the time when it would otherwise be advantageous to do so. It is anticipated that unrealized gains on futures contracts, which have been open for less than three months as of the end of the Fund's fiscal year and which are recognized for tax purposes, will not be considered gains on securities held less than three months for the purpose of the 30% test.

The Fund will distribute to shareholders annually any net capital gains which have been recognized for federal income tax purposes (including unrealized gains at the end of the Fund's fiscal year) on futures transactions. Such distributions will be combined with distributions of capital gains realized on the Fund's other investments and shareholders will be advised on the nature of the payments.

RESTRICTED SECURITIES The Fund is authorized to invest up to 15% of its net assets in restricted securities. Restricted securities are those which are

not registered under the Securities Act of 1933 and which are generally issued in small quantities to institutional or individual investors. Restricted securities can be sold only in a privately negotiated transaction or after the filing of a registration statement. The market for such securities is generally illiquid.

If the Fund chooses to sell a restricted security by filing a registration statement, the filing may involve a considerable delay, during which time the market value of the security may decline. Because of the illiquid market for restricted securities, the announcement of the Fund's decision to sell a restricted security may also depress the security's price. In certain cases, the Fund may also be obligated to pay all or part of the security's registration expenses, which may be substantial.

4

5

PURCHASE OF SHARES

The purchase price of shares of the Fund is the net asset value next determined after the order is received. The net asset value is calculated as of the close of the New York Stock Exchange on each day the Exchange is open for business. An order received prior to the close of the Exchange (generally 4:00 P.M. Eastern time) will be executed at the price computed on the date of receipt, and an order received after the close of the Exchange will be executed at the price computed on the next day the Exchange is open.

The Fund reserves the right in its sole discretion (i) to suspend the offering of its shares, (ii) to reject purchase orders when in the judgment of management such rejection is in the best interests of the Fund, and (iii) to reduce or waive the minimum for initial and subsequent investments for certain fiduciary accounts such as employee benefit plans or under circumstances where certain economies can be achieved in sales of the Fund's shares.

REDEMPTION OF SHARES

The Fund may suspend redemption privileges or postpone the date of payment (i) during any period that the New York Stock Exchange is closed, or trading on the Exchange is restricted as determined by the Securities and Exchange Commission (the "Commission"), (ii) during any period when an emergency exists as defined by the rules of the Commission as a result of which it is not reasonably practicable for the Fund to dispose of securities owned by it, or fairly to determine the value of its assets, and (iii) for such other periods as the Commission may permit.

The Fund has made an election with the Commission to pay in cash all redemptions requested by any shareholder of record limited in amount during any 90-day period to the lesser of \$250,000 or 1% of the net assets of the Fund at the beginning of such period. Such commitment is irrevocable without the prior approval of the Commission. Redemptions in excess of the above limits may be paid in whole or in part in readily marketable investment securities or in cash, as the Directors may deem advisable; however, payment will be made wholly in cash unless the Directors believe that economic or market conditions exist which would make such a practice detrimental to the best interests of the Fund. If redemptions are paid in investment securities, such securities will be valued as set forth in the Prospectus under "The Fund's Share Price" and a redeeming shareholder would normally incur brokerage expenses if these securities were converted to cash.

No charge is made by the Fund for redemptions. Any redemption may be more or less than the shareholder's cost depending on the market value of the Fund's portfolio securities.

DIVIDENDS AND CAPITAL GAINS DISTRIBUTIONS

The Fund's policy is to distribute annually substantially all of its net investment income, if any, together with any net realized capital gains, after the close of the Fund's fiscal year. Dividend income is expected to be negligible, and the amount of any capital gains distributions cannot be predicted.

Any dividend or distribution paid shortly after the purchase of shares by an investor may have the effect of reducing the per share net asset value by the per share amount of the dividend or distribution. Furthermore, such dividends or distributions, although in effect a return of capital, are subject to income taxes.

Unless the shareholder elects otherwise, dividends and capital gains distributions are paid in additional shares which are credited to the shareholder's account. Any dividend and distribution election will remain in effect until the Fund's Transfer Agent is notified by the shareholder in writing to change the election at least three days prior to the record date. An account statement is sent to shareholders whenever an income dividend or capital gains distribution is paid.

5

6

YIELD AND TOTAL RETURN

The yield of the Fund for the thirty-day period ended October 31, 1994 was 0.31%.

The average annual total returns for the Fund for the one-, five- and ten-year periods ending October 31, 1994, were +4.49%, +12.87% and +9.70%, respectively. Total return is computed by determining the average compounded rates of return over the one-, five- and ten-year periods set forth above that would equate an initial amount invested at the beginning of the periods to the ending redeemable value of the investment.

INVESTMENT LIMITATIONS

The Fund is subject to the following restrictions which may not be changed without the approval of the lesser of (i) 67 percent or more of the voting securities present at a meeting if the holders of more than 50 percent of the outstanding voting securities of the Fund are present or represented by proxy, or (ii) more than 50 percent of the outstanding voting securities of the Fund. The Fund will not:

- 1) make investments in commodities or real estate, although it may purchase and sell securities of companies which deal in real estate or interests therein, and except that the Fund may invest in stock futures contracts and stock options (only for hedging purposes) to the extent that not more than 5% of its assets are required as deposit to secure obligations under futures contracts and not more than 20% of its assets are invested in futures contracts and options at any time;
- 2) make loans, except (i) by purchasing bonds, debentures or similar obligations (including repurchase agreements) which are either publicly distributed or customarily purchased by institutional investors and (ii) as provided under "Lending of Securities" (page 2);
- 3) engage in the business of underwriting securities issued by others except to the extent that the Fund may technically be deemed to be an underwriter under the Securities Act of 1933, as amended, in disposing of portfolio securities;
- 4) purchase or otherwise acquire illiquid securities if, as a result, more than 15% of its net assets would be invested in securities that are illiquid (included in this limitation is the Fund's investment in The Vanguard Group, Inc.);
- 5) purchase securities on margin or make short sales except as specified in investment limitation No. 1 above;
- 6) invest more than 25% of its assets in any one industry;
- 7) invest for the purpose of exercising control over management of any company;
- 8) invest its assets in the securities of other investment companies except as may be acquired as part of a merger, consolidation or acquisition of assets approved by the Fund's shareholders or otherwise to the extent permitted by Section 12 of the Investment Company Act of 1940. The Fund will invest only in investment companies which have investment objectives and investment policies consistent with those of the Fund;
- 9) with respect to 75% of the value of its total assets, purchase the securities of any issuer (except obligations of the United States government and its instrumentalities) if as a result the Fund would hold more than 10% of the outstanding voting securities of the issuer,

or more than 5% of the value of the Fund's total assets would be invested in the securities of such issuer;

- 10) pledge, mortgage, or hypothecate any of its assets to an extent greater than 10% of its total assets at fair market value;
- 11) invest more than 25% of the value of its total assets in any one industry; and
- 12) borrow money, except that the Fund may borrow from banks (or through reverse repurchase agreements), for temporary or emergency (not leveraging) purposes, including the meeting of redemption requests which might otherwise require the untimely disposition of securities, in an amount not

6

7

exceeding 15% of the value of the Fund's net assets (including the amount borrowed and the value of any outstanding reverse repurchase agreements) at the time the borrowing is made. Whenever borrowings exceed 5% of the value of the Fund's net assets, the Fund will not make any additional investments.

Notwithstanding these limitations, the Fund may own all or any portion of the securities of, or make loans to, or contribute to the costs or other financial requirements of any company which will be wholly owned by the Fund and one or more other investment companies and is primarily engaged in the business of providing, at-cost, management, administrative or related services to the Fund and other investment companies. See "Management of the Fund."

The above-mentioned limitations are considered at the time investment securities are purchased.

Although not a fundamental policy subject to shareholder vote, as long as the Fund's shares are registered for sale in certain states, the Fund will not (i) except as permitted above in investment limitation No. 1; (ii) invest in interests in oil, gas or other mineral exploration or development programs; (iii) purchase securities of any company which has (with predecessors) a record of less than three years continuous operation if as a result more than 5% of the Fund's assets would be invested in securities of such companies; and (iv) purchase or retain securities of an issuer if an officer or director of such issuer is an officer or Director of the Fund or its investment adviser and one or more of such officers or Directors of the Fund or its investment adviser owns beneficially more than 1/2% of the shares or securities of such issuer and all such Directors and officers owning more than 1/2% of such shares or securities together own more than 5% of such shares or securities.

7

8

MANAGEMENT OF THE FUND

OFFICERS AND DIRECTORS

The Fund's Officers, under the supervision of the Board of Directors, manage the day-to-day operations of the Fund. The Directors, who are elected annually by shareholders, set broad policies for the Fund and choose its Officers. A list of the Directors and Officers of the Fund and a brief statement of their present positions and principal occupations during the past five years is set forth below.

The mailing address of the Fund's Directors and officers is Post Office Box 876, Valley Forge, PA 19482.

JOHN C. BOGLE, Chairman, Chief Executive Officer and Director*
Chairman, Chief Executive Officer, and Director of The Vanguard Group, Inc. and of each of the investment companies in The Vanguard Group; Director of The Mead Corporation, and General Accident Insurance.

JOHN J. BRENNAN, President & Director*
President and Director of The Vanguard Group, Inc. and of each of the investment companies in The Vanguard Group.

ROBERT E. CAWTHORN, Director

Chairman of Rhone-Poulenc Rorer, Inc.; Director of Sun Company, Inc.

BARBARA BARNES HAUPTFUHRER, Director

Director of The Great Atlantic and Pacific Tea Company, ALCO Standard Corp., Raytheon Company, Knight-Ridder, Inc., and Massachusetts Mutual Life Insurance Co. and Trustee Emerita of Wellesley College.

BRUCE K. MACLAURY, Director

President, The Brookings Institution; Director of American Express Bank, Ltd., The St. Paul Companies, Inc., and Scott Paper Company.

BURTON G. MALKIEL, Director

Chemical Bank Chairman's Professor of Economics, Princeton University; Director of Prudential Insurance Co. of America, Amdahl Corporation, Baker Fentress & Co., The Jeffrey Co., and Southern New England Communications Company.

ALFRED M. RANKIN, JR., Director

Chairman, President, and Chief Executive Officer of NACCO Industries, Inc.; Director of The BFGoodrich Company, The Standard Products Company and The Reliance Electric Company.

JOHN C. SAWHILL, Director

President and Chief Executive Officer, The Nature Conservancy; formerly, Director and Senior Partner, McKinsey & Co.; President, New York University; Director of Pacific Gas and Electric Company and NACCO Industries.

JAMES O. WELCH, JR., Director

Retired Chairman of Nabisco Brands, Inc. retired Vice Chairman and Director of RJR Nabisco; Director of TECO Energy, Inc.

J. LAWRENCE WILSON, Director

Chairman and Chief Executive Officer of Rohm & Haas Company; Director of Cummins Engine Company; Trustee of Vanderbilt University and the Culver Educational Foundation.

RAYMOND J. KLAPINSKY, Secretary*

Senior Vice President and Secretary of The Vanguard Group, Inc.; Secretary of each of the investment companies in The Vanguard Group.

RICHARD F. HYLAND, Treasurer*

Treasurer of The Vanguard Group, Inc. and of each of the investment companies in The Vanguard Group.

KAREN E. WEST, Controller*

Vice President of The Vanguard Group, Inc.; Controller of each of the investment companies in The Vanguard Group.

*Officers of the Fund are "interested persons" as defined in the Investment Company Act of 1940.

VANGUARD GROUP

Vanguard Explorer Fund is a member of The Vanguard Group of Investment Companies, which consists of more than 30 investment companies. Through their jointly-owned subsidiary, The Vanguard Group, Inc. ("Vanguard"), the Fund and the other Funds in the Group obtain at cost virtually all of their corporate

management, administrative and distribution services. Vanguard also provides investment advisory services on an at-cost basis to some of the Vanguard Funds.

Vanguard employs a supporting staff of management and administrative personnel needed to provide the requisite services to the Funds and also furnishes the Funds with necessary office space, furnishings and equipment. Each Fund pays its share of Vanguard's total expenses, which are allocated among the Funds under procedures approved by the Board of Directors (Trustees) of each Fund. In addition, each Fund bears its own direct expenses, such as legal, auditing and custodian fees.

The Fund's Officers are also Officers and employees of Vanguard. No Officer or employee owns, or is permitted to own, any securities of any external adviser

for the Funds.

The Vanguard Group adheres to a Code of Ethics established pursuant to Rule 17j-1 under the Investment Company Act of 1940. The Code is designed to prevent unlawful practices in connection with the purchase or sale of securities by persons associated with Vanguard. Under Vanguard's Code of Ethics certain officers and employees of Vanguard who are considered access persons are permitted to engage in personal securities transactions. However, such transactions are subject to procedures and guidelines substantially similar to those recommended by the mutual fund industry and approved by the U.S. Securities and Exchange Commission.

The Vanguard Group was established and operates under a Funds' Service Agreement which was approved by the shareholders of each of the Funds. The Fund's Service Agreement was amended on May 15, 1993 to provide as follows: (a) each Vanguard Fund may invest up to .40% of its current net assets in Vanguard, and (b) there is no limit on the amount that each Vanguard Fund may contribute to Vanguard's capitalization. The amounts which each of the Funds have invested are adjusted from time to time in order to maintain the proportionate relationship between each Fund's relative net assets and its contribution to Vanguard's capital. At October 31, 1994, Vanguard Explorer Fund had contributed capital of \$169,000 to Vanguard, representing .8% of Vanguard's capitalization.

MANAGEMENT Corporate management and administrative services include: (1) executive staff; (2) accounting and financial; (3) legal and regulatory; (4) shareholder account maintenance; (5) monitoring and control of custodian relationships; (6) shareholder reporting; and (7) review and evaluation of advisory and other services provided to the Funds by third parties. During the fiscal year ended October 31, 1994, the Fund's share of Vanguard's actual net costs of operation relating to management and administrative services (including transfer agency) totaled approximately \$3,472,000.

DISTRIBUTION Vanguard provides all distribution and marketing activities for the Funds in the Group. Vanguard Marketing Corporation, a wholly-owned subsidiary of The Vanguard Group, Inc., acts as Sales Agent for shares of the Funds, in connection with any sales made directly to investors in the states of Florida, Missouri, New York, Ohio, Texas and such other states as it may be required.

The principal distribution expenses are for advertising, promotional materials and marketing personnel. Distribution services may also include organizing and offering to the public, from time to time, one or more new investment companies which will become members of the Group. The Directors and officers of Vanguard determine the amount to be spent annually on distribution activities, the manner and amount to be spent on each Fund, and whether to organize new investment companies.

One half of the distribution expenses of a marketing and promotional nature is allocated among the Funds based upon their relative net assets. The remaining one half of these expenses is allocated among the Funds based upon each Fund's sales for the preceding 24 months relative to the total sales of the Funds as a Group, provided, however, that no Fund's aggregate quarterly rate of contribution for distribution expenses of a marketing and promotional nature shall exceed 125% of the average distribution expense rate for the Group, and that no Fund shall incur annual distribution expenses in excess of 20/100 of 1% of its average month-end net assets. During the fiscal year ended October 31, 1994, the Fund paid approximately \$170,000 of the Group's distribution and marketing expenses, which represented an effective annual rate of .02 of 1% of the Fund's average net assets.

9

10

INVESTMENT ADVISORY SERVICES Vanguard also provides investment advisory services to: Vanguard Money Market Reserves; Vanguard Municipal Bond Fund, several Portfolios of Vanguard Fixed Income Securities Fund; Vanguard Bond Index Fund; Vanguard California Tax-Free Fund; Vanguard New Jersey Tax-Free Fund; Vanguard Florida Insured Tax-Free Fund; Vanguard New York Insured Tax-Free Fund; Vanguard Pennsylvania Tax-Free Fund; Vanguard Ohio Tax-Free Fund; Vanguard Institutional Money Market Portfolio; Vanguard Index Trust; Vanguard International Equity Index Fund; Vanguard Balanced Index Fund; Vanguard Institutional Index Fund; several Portfolios of Vanguard Variable Insurance Fund, Vanguard Admiral Funds, Vanguard Tax-Managed Fund, Vanguard Horizon Fund, a portion of Vanguard/Windsor II, a portion of Vanguard/Morgan Growth Fund as well as several indexed separate accounts. These services are provided on an at-cost basis from a money management staff employed directly by Vanguard. The

compensation and other expenses of this staff are paid by the Funds utilizing these services.

REMUNERATION OF DIRECTORS AND OFFICERS The Fund pays each Director, who is not also an Officer, an annual fee plus travel and other expenses incurred in attending Board meetings. The Fund's Officers and employees are paid by Vanguard which, in turn, is reimbursed by the Fund, and each other Fund in the Group, for its proportionate share of Officers' and employees' salaries and retirement benefits.

Under its retirement plan, Vanguard contributes annually an amount equal to 10% of each eligible Officer's annual compensation plus 7% of that part of the eligible Officer's compensation during the year, if any, that exceeds the Social Security Taxable Wage Base then in effect. Under Vanguard's thrift plan, all eligible Officers are permitted to make pre-tax basic contributions in a maximum amount equal to 4% of total compensation which are matched by Vanguard on a 100% basis. Directors who are not Officers are paid an annual fee based on the number of years of service on the board, up to 15 years of service, upon retirement. The fee is equal to \$1,000 for each year of service and each investment company member of The Vanguard Group contributes a proportionate amount to this fee based on its relative net assets. This fee is paid, subsequent to a Director's retirement, for a period of ten years or until the death of a retired Director.

The following table provides detailed information with respect to the amounts paid or accrued for the Directors, and the Officers of the Fund for whom the Fund's proportionate share of remuneration exceeded \$60,000, for the fiscal year ended October 31, 1994.

VANGUARD EXPLORER FUND

COMPENSATION TABLE

<TABLE>
<CAPTION>

NAMES OF DIRECTORS	AGGREGATE COMPENSATION FROM FUND	PENSION OR RETIREMENT BENEFITS ACCRUED AS PART OF FUND EXPENSES	ESTIMATED ANNUAL BENEFITS UPON RETIREMENT	TOTAL COMPENSATION FROM ALL VANGUARD FUNDS PAID TO DIRECTORS (2)
<S>	<C>	<C>	<C>	<C>
John C. Bogle(1)	--	--	--	--
John J. Brennan(1)	--	--	--	--
Barbara Barnes Hauptfuhrer	\$333	\$67	\$15,000	\$50,000
Robert E. Cawthorn	\$333	\$56	\$13,000	\$50,000
Bruce K. MacLaury	\$299	\$56	\$12,000	\$45,000
Burton G. Malkiel	\$333	\$45	\$15,000	\$50,000
Alfred M. Rankin, Jr.	\$333	\$36	\$15,000	\$50,000
John C. Sawhill	\$333	\$42	\$15,000	\$50,000
James O. Welch, Jr.	\$319	\$52	\$15,000	\$48,000
J. Lawrence Wilson	\$326	\$37	\$15,000	\$49,000

</TABLE>

(1)As "Interested Directors," Messrs. Bogle and Brennan receive no compensation for their service as directors. Compensation amounts reported for Messrs. Bogle and Brennan relate to their respective positions as Chief Executive Officer and President of the Fund.

(2)The amounts reported in this column reflect the total compensation paid to each Director for their service as Director or Trustee of 33 Vanguard Funds (32 in the case of Mr. MacLaury).

INVESTMENT ADVISORY SERVICES

The Fund currently employs two investment advisers: Wellington Management Company ("WMC"), 75 State Street, Boston, MA 02109; and Granahan Investment Management, Inc. ("Granahan"), 303 Wyman Street, Waltham, MA 02154. Until February 28, 1990, when the Fund acquired the assets of Explorer II, WMC was sole investment adviser to the Fund (then known simply as Explorer Fund), and Granahan served as sole investment adviser to Explorer II, the acquired fund.

The proportion of the net assets of the Fund managed by each adviser was established by the Board of Directors effective with the acquisition of Explorer II, and may be changed in the future by the Board of Directors as circumstances warrant. Investors will be advised of any substantive change in the proportions managed by each adviser. Because the Fund employs two advisers it is possible that the advisers would purchase or sell the same security at the same time. Such a situation might result in increased brokerage costs or adverse tax consequences to the Fund. The Board of Directors monitors portfolio activity in order to minimize any possible adverse consequences.

WELLINGTON MANAGEMENT COMPANY

The Fund has entered into an advisory agreement with WMC under which WMC manages the investment and reinvestment of a portion of the Fund's assets (the "WMC Portfolio") and continuously reviews, supervises and administers the Fund's investment program with respect to those assets. As of October 31, 1994, WMC managed approximately 48% of the Fund's net assets. WMC discharges its responsibilities subject to the control of the officers and Directors of the Fund.

WMC is a professional investment counseling firm which provides investment services to investment companies, other institutions and individuals. WMC is a Massachusetts general partnership of which the following persons are managing partners: Robert W. Doran, Duncan M. McFarland and John B. Neff.

The Fund pays WMC a Basic Fee at the end of each fiscal quarter, calculated by applying a quarterly rate, based on the following annual percentage rates, to the average month-end net assets of the WMC Portfolio for the quarter:

<TABLE>
<CAPTION>

NET ASSETS	RATE
-----	-----
<S>	<C>
First \$100 million	0.35%
Next \$250 million	0.30%
Over \$350 million	0.25%

</TABLE>

The Basic Fee paid to WMC may be increased or decreased by applying an adjustment formula based on the investment performance of the net assets of the WMC Portfolio. Such formula provides for an increase or decrease in WMC's Basic Fee in an amount equal to .075% per annum (.01875 of 1% per quarter) of the average month-end net assets of the WMC Portfolio if the investment performance of the WMC Portfolio for the thirty-six months preceding the end of the quarter is twelve percentage points or more above or below, respectively, the investment record of the Russell 2000 Small Company Index (the "Russell 2000") for the same period; or by an amount equal to .0375% per annum (.009375 of 1% per quarter) if the investment performance of the WMC Portfolio for such thirty-six months is six or more but less than twelve percentage points above or below, respectively, the investment record of the Russell 2000 for the same period. The incentive portion of the fee may be earned even if the performance of the WMC Portfolio for the period is negative provided that the Portfolio's performance exceeds the Russell 2000 by the required percentage.

The investment performance of the WMC Portfolio for any period, expressed as a percentage of the "WMC Portfolio unit value" at the beginning of such period, is the sum of: (i) the change in the WMC Portfolio unit value during such period; (ii) the unit value of the Fund's cash distributions from the WMC Portfolio net investment income and realized net capital gains (whether long-term or short-term) having an ex-dividend date occurring within such period; and (iii) the unit value of capital gains taxes paid or accrued during such period by the Fund for undistributed realized long-term capital gains realized from the WMC Portfolio.

The "WMC Portfolio unit value" is determined by dividing the total net assets of the WMC Portfolio by a given number of units. On the initial date of the agreement, the number of units in the WMC Portfolio will equal the total shares outstanding of the Fund. After such initial date, as assets are added to or are withdrawn from the WMC Portfolio, the number of units of the WMC Portfolio is adjusted based on the unit value of the WMC Portfolio on the day such changes are executed.

The investment record of the Russell 2000 for any period, expressed as a percentage of the Russell 2000 at the beginning of such period, is the sum of (i) the change in the level of the Russell 2000 during such period and (ii) the value, computed consistently with the Russell 2000, of cash distributions having an ex-dividend date occurring within such period made by companies whose securities comprise the Russell 2000. For this purpose cash distributions on the securities which comprise the Russell 2000 shall be treated as reinvested in the Russell 2000 at least as frequently as the end of each calendar quarter following the payment of the dividend.

For the purposes of determining the fee adjustment for investment performance, the net assets of the WMC Portfolio are averaged over the same period as the investment performance of the WMC Portfolio and the investment record of the Russell 2000 are computed.

Any computation of the investment performance of the WMC Portfolio and the investment record of the Russell 2000 shall be subject to and in accordance with any then applicable rules of the Securities and Exchange Commission.

During the fiscal years ended October 31, 1992, 1993, and 1994, the Fund paid WMC approximately the following advisory fees:

<TABLE>

<CAPTION>

	1992	1993	1994
	-----	-----	-----
<S>	<C>	<C>	<C>
Basic Fee.....	\$ 918,671	\$1,181,674	\$1,362,455
Increase (Decrease) for Performance Adjustment.....	82,994	(79,280)	(61,905)
	-----	-----	-----
Total.....	\$1,001,665	\$1,102,394	\$1,300,550
	=====	=====	=====

</TABLE>

The agreement with WMC continues until February 27, 1995. The agreement is renewable thereafter, for successive one year periods, only if each renewal is specifically approved by a vote of the Fund's Board of Directors, including the affirmative votes of a majority of the Directors who are not parties to the contract or "interested persons" (as defined in the Investment Company Act of 1940) of any such party, cast in person at a meeting called for the purpose of considering such approval. In addition, the question of continuance of the agreement may be presented to the shareholders of the Fund; in such event continuance shall be effected only if approved by the affirmative vote of a majority of the outstanding voting securities of the Fund. The agreement is automatically terminated if assigned, and may be terminated without penalty at any time (1) either by vote of the Board of Directors of the Fund or by vote of its outstanding voting securities on sixty (60) days' written notice to WMC, or (2) by WMC upon ninety (90) days' written notice to the Fund.

GRANAHAN INVESTMENT MANAGEMENT, INC.

On February 28, 1990, effective with the acquisition of the assets of Explorer II, the Fund retained Granahan Investment Management, Inc. ("Granahan") as a second investment adviser. Under its advisory agreement with the Fund, Granahan manages the investment and reinvestment of a portion of the Fund's assets (the "Granahan Portfolio") and continuously reviews, supervises and administers the Fund's investment program with respect to those assets. As of October 31, 1994, Granahan managed approximately 47% of the Fund's net assets. Granahan discharges its responsibilities subject to the control of the officers and Directors of the Fund.

The Fund pays Granahan a Basic Fee at the end of each fiscal quarter,

calculated by applying a quarterly rate, based on the following annual percentage rates, to the average month-end net assets of the Granahan Portfolio for the quarter:

<TABLE>
<CAPTION>

NET ASSETS	RATE
-----	-----
<S>	<C>
First \$50 million	0.45%
Next \$50 million	0.40%
Next \$100 million	0.35%
Over \$200 million	0.25%

</TABLE>

The Basic Fee paid to Granahan may be increased or decreased by applying an adjustment formula based on the investment performance of the net assets of the Granahan Portfolio. Such formula provides for an increase or decrease in Granahan's Basic Fee in an amount equal to .075% per annum (.01875 of 1% per quarter) of the average month-end net assets of the Granahan Portfolio if the investment performance of the Granahan Portfolio for the thirty-six months preceding the end of the quarter is twelve percentage points or more above or below, respectively, the investment record of the Russell 2000 Small Company Index (the "Russell 2000") for the same period; or by an amount equal to .0375% per annum (.009375 of 1% per quarter) if the investment performance of the Granahan Portfolio for such thirty-six months is six or more but less than twelve percentage points above or below, respectively, the investment record of the Russell 2000 for the same period. The incentive portion of the fee may be earned even if the performance of the Granahan Portfolio for the period is negative provided that the Portfolio's performance exceeds the Russell 2000 by the required percentage.

The investment performance of the Granahan Portfolio for any period, expressed as a percentage of the "Granahan Portfolio unit value" at the beginning of such period, is the sum of: (i) the change in the Granahan Portfolio unit value during such period; (ii) the unit value of the Fund's cash distributions from the Granahan Portfolio net investment income and realized net capital gains (whether long-term or short-term) having an ex-dividend date occurring within such period; and (iii) the unit value of capital gains taxes paid or accrued during such period by the Fund for undistributed realized long-term capital gains realized from the Granahan Portfolio.

The "Granahan Portfolio unit value" is determined by dividing the total net assets of the Granahan Portfolio by a given number of units. On the initial date of the agreement, the number of units in the Granahan Portfolio equalled the total shares outstanding of the Fund. After such initial date, as assets are added to or are withdrawn from the Granahan Portfolio, the number of units of the Granahan Portfolio is adjusted based on the unit value of the Granahan Portfolio on the day such changes are executed.

The investment record of the Russell 2000 for any period, expressed as a percentage of the Russell 2000 at the beginning of such period, is the sum of (i) the change in the level of the Russell 2000 during such period and (ii) the value, computed consistently with the Russell 2000, of cash distributions having an ex-dividend date occurring within such period made by companies whose securities comprise the Russell 2000. For this purpose cash distributions on the securities which comprise the Russell 2000 shall be treated as reinvested in the Russell 2000 at least as frequently as the end of each calendar quarter following the payment of the dividend.

For the purposes of determining the fee adjustment for investment performance, the net assets of the Granahan Portfolio are averaged over the same period as the investment performance of the Granahan Portfolio and the investment record of the Russell 2000 are computed.

Any computation of the investment performance of the Granahan Portfolio and the investment record of the Russell 2000 shall be subject to and in accordance with any then applicable rules of the Securities and Exchange Commission.

During the fiscal years ended October 31, 1992, 1993 and 1994, the Fund paid Granahan approximately the following advisory fees:

<TABLE>

<CAPTION>

	1992	1993	1994
<S>	<C>	<C>	<C>
Basic Fee.....	\$673,252	\$ 936,872	\$1,397,812
Increase (Decrease) for Performance Adjustment.....	87,536	116,432	40,525
Total.....	\$760,788	\$1,053,304	\$1,438,337

</TABLE>

The agreement continues until February 27, 1995 and will be renewable thereafter for successive one year periods, only if each renewal is specifically approved by a vote of the Fund's Board of Directors, including the affirmative votes of a majority of the Directors who are not parties to the contract or "interested persons" (as defined in the Investment Company Act of 1940) of any such party, cast in person at a meeting called for the purpose of considering such approval. In addition, the question of continuance of the agreement may be presented to the shareholders of the Fund; in such event, such continuance shall be effected only if approved by the affirmative vote of a majority of the outstanding voting securities of the Fund. The agreement is automatically terminated if assigned, and may be terminated without penalty at any time (1) either by vote of the Board of Directors of the Fund or by vote of its outstanding voting securities on 60 days' written notice to Granahan, or (2) by Granahan upon 90 days' written notice to the fund.

In April 1972, the Securities and Exchange Commission ("SEC") issued Release No. 7113 under the Investment Company Act of 1940 to call attention of directors and investment advisers to certain factors which must be considered in connection with investment company incentive fee arrangements. One of these factors is to "avoid basing significant fee adjustments upon random or insignificant differences" between the investment performance of a fund and that of the particular index with which it is being compared. The Release provides that "preliminary studies (of the SEC staff) indicate that as a 'rule of thumb' the performance difference should be at least 10 percentage points" annually before the maximum performance adjustment may be made. However, the Release also states that "because of the preliminary nature of these studies, the Commission is not recommending, at this time, that any particular performance difference exist before the maximum fee adjustment may be made." The Release concludes that the directors of a fund "should satisfy themselves that the maximum performance adjustment will be made only for performance differences that can reasonably be considered "significant." The Board of Directors of Vanguard Explorer Fund has fully considered the SEC Release and believes that the performance adjustments as included in the above mentioned agreements are appropriate, although not within the 10 percentage point per year range suggested in the Release. Under the proposed investment advisory agreement between Vanguard Explorer Fund and Granahan, and Vanguard Explorer Fund and WMC, the maximum performance adjustment is made at a difference of 12 percentage points from the performance of the index over a thirty-six month period, which would effectively be the equivalent of approximately 4 percentage points difference per year.

The Fund's Board of Directors may, without the approval of shareholders, provide for:

- A. The employment of a new investment adviser pursuant to the terms of a new advisory agreement, either as a replacement for an existing adviser or as an additional adviser.
- B. A change in the terms of an advisory agreement.
- C. The continued employment of an existing adviser on the same advisory contract terms where a contract has been assigned because of a change in control of the adviser.

Any such change will only be made upon not less than 30 days prior written notice to shareholders, which shall include the information concerning the adviser that would have normally been included in a proxy statement.

PORTFOLIO TRANSACTIONS

The investment advisory agreements authorize WMC and Granahan (with the approval of the Fund's Board of Directors) to select the brokers or dealers that

will execute the purchases and sales of portfolio securities for the Fund and direct the advisers to use their best efforts to obtain the best available price and most favorable execution as to all transactions for the Fund. WMC and Granahan have undertaken to execute each investment transaction at a price and commission which provides the most favorable total cost or proceeds reasonably obtainable under the circumstances.

In placing portfolio transactions, WMC and Granahan will use their best judgment to choose the broker most capable of providing the brokerage services necessary to obtain best available price and most favorable execution. The full range and quality of brokerage services available will be considered in making these determinations. In those instances where it is reasonably determined that more than one broker can offer the brokerage services needed to obtain the best available price and most favorable execution, consideration may be given to those brokers which supply investment research and statistical information and provide other services in addition to execution services to the Fund and/or WMC or Granahan. WMC and Granahan consider such information useful in the performance of its obligations under the agreement but are unable to determine the amount by which such services may reduce its expenses.

The investment advisory agreement also incorporates the concepts of Section 28(e) of the Securities Exchange Act of 1934 by providing that, subject to the approval of the Fund's Board of Directors, WMC and Granahan may cause the Fund to pay a broker-dealer which furnishes brokerage and research services a higher commission than that which might be charged by another broker-dealer for effecting the same transaction; provided that such commission is deemed reasonable in terms of either that particular transaction or the overall responsibilities of WMC and Granahan to the Fund and the other Funds in the Group.

Currently, it is the Fund's policy that WMC and Granahan may at times pay higher commissions in recognition of brokerage services felt necessary for the achievement of better execution of certain securities transactions that otherwise might not be available. The advisers will only pay such higher commissions if they believe this to be in the best interest of the Fund. Some brokers or dealers who may receive such higher commissions in recognition of brokerage services related to execution of securities transactions are also providers of research information to WMC, Granahan and/or the Fund.

Since the Fund does not market its shares through intermediary brokers or dealers, it is not the Fund's practice to allocate brokerage or principal business on the basis of sales of its shares which may be through such firms. However, the Fund may place portfolio orders with qualified broker-dealers who recommend the Fund to other clients, or who act as agent in the purchase of the Fund's shares for their clients, and may, when a number of brokers and dealers can provide comparable best price and execution on a particular transaction, consider the sale of Fund shares by a broker or dealer in selecting among qualified broker-dealers.

During the fiscal years ended October 31, 1992, 1993 and 1994 the Fund paid \$336,169, \$452,558 and \$1,627,910 in brokerage commissions, respectively.

Some securities considered for investment by the Fund may also be appropriate for other Funds and/or clients served by WMC or Granahan. If purchase or sale of securities consistent with the investment policies of the Fund and one or more of these other Funds or clients served by the advisers are considered at or about the same time, transactions in such securities will be allocated among the several Funds and clients in a manner deemed equitable by WMC or Granahan.

GENERAL INFORMATION ABOUT THE FUND

DESCRIPTION OF SHARES AND VOTING RIGHTS

The Fund was established under Pennsylvania law under a Declaration of Trust dated April 17, 1984. The Fund was reorganized as a Maryland corporation on December 31, 1986. On February 28, 1990, the Fund acquired the assets of Explorer II, Inc., an investment company that was a member of The Vanguard Group

and that had investment objectives and policies similar to those of the Fund. Also, on that date the Fund retained Granahan Investment Management Inc., investment adviser to Explorer II, as the Fund's second adviser and adopted its new name.

The Fund's Amended and Restated Articles of Incorporation permit the Directors to issue 100,000,000 shares of common stock, with a \$.001 par value. The Board of Directors has the power to designate one or more classes ("Portfolios") of shares of common stock and to classify or reclassify any unissued shares with respect to such Portfolios. Currently, the Fund is offering one class of shares.

The shares of the Fund are fully paid and nonassessable, and have no preferences as to conversion, exchange, dividends, retirement or other features. The shares have no pre-emptive rights. Such shares have non-cumulative voting rights, which means that the holders of more than 50% of the shares voting for the election of Directors can elect 100% of the Directors if they choose to do so. A shareholder is entitled to one vote for each full share held (and a fractional vote for each fractional share held), then standing in his name on the books of the Fund.

PERFORMANCE MEASURES

The Fund may use one or more, either singularly or in a composite, of the following unmanaged indexes for comparative performance purposes:

STANDARD & POOR'S 500 COMPOSITE STOCK PRICE INDEX -- is a well-diversified list of 500 companies representing the U.S. Stock Market.

WILSHIRE 5000 EQUITY INDEX -- consists of more than 6,000 common equity securities, covering all stocks in the U.S. for which daily pricing is available.

WILSHIRE 4500 EQUITY INDEX -- consists of all stocks in the Wilshire 5000 except for the 500 stocks in the Standard & Poor's 500 Index.

MORGAN STANLEY CAPITAL INTERNATIONAL EAFE INDEX -- is an arithmetic, market value-weighted average of the performance of over 900 securities listed on the stock exchanges of countries in Europe, Australia and the Far East.

GOLDMAN SACHS 100 CONVERTIBLE BOND INDEX -- currently includes 67 bonds and 33 preferreds. The original list of names was generated by screening for convertible issues of 100 million or greater in market capitalization. The index is priced monthly.

SALOMON BROTHERS GNMA INDEX -- includes pools of mortgages originated by private lenders and guaranteed by the mortgage pools of the Government National Mortgage Association.

SALOMON BROTHERS HIGH-GRADE CORPORATE BOND INDEX -- consists of publicly issued, non-convertible corporate bonds rated AA or AAA. It is a value-weighted, total return index, including approximately 800 issues with maturities of 12 years or greater.

LEHMAN LONG-TERM TREASURY BOND -- is composed of all bonds covered by the Shearson Lehman Hutton Treasury Bond Index with maturities of 10 years or greater.

MERRILL LYNCH CORPORATE & GOVERNMENT BOND -- consists of over 4,500 U.S. Treasury, Agency and investment grade corporate bonds.

LEHMAN CORPORATE (BAA) BOND INDEX -- all publicly offered fixed rate, nonconvertible domestic corporate bonds rated Baa by Moody's, with a maturity longer than 1 year and with more than \$25 million outstanding. This index includes over 1,000 issues.

BOND BUYER MUNICIPAL INDEX (20 YEAR) BOND -- is a yield index on current coupon high grade general obligation municipal bonds.

STANDARD & POOR'S PREFERRED INDEX -- is a yield index based upon the average yield of four high grade, noncallable preferred stock issues.

NASDAQ INDUSTRIAL INDEX -- is composed of more than 3,000 industrial issues. It is a value-weighted index calculated on price change only and does not include income.

COMPOSITE INDEX -- 70% Standard & Poor's 500 Index and 30% NASDAQ Industrial

Index.

COMPOSITE INDEX -- 35% Standard & Poor's 500 Index and 65% Salomon Brothers High-Grade Bond Index.

COMPOSITE INDEX -- 65% Standard & Poor's 500 Index and 35% Salomon Brothers High-Grade Bond Index.

LEHMAN BROTHERS AGGREGATE BOND INDEX -- is a market weighted index that contains individually priced U.S. Treasury, agency, corporate, and mortgage pass through securities corporate rated BBB- or better. The index has a market value of over \$4 trillion.

LEHMAN BROTHERS MUTUAL FUND SHORT (1-5) GOVERNMENT/CORPORATE INDEX -- is a market weighted index that contains individually priced U.S. Treasury, agency, and corporate investment grade bonds rated BBB- or better with maturities between 1 and 5 years. The index has a market value of over \$1.3 trillion.

LEHMAN BROTHERS MUTUAL FUND INTERMEDIATE (5-10) GOVERNMENT/CORPORATE INDEX -- is a market weighted index that contains individually priced U.S. Treasury, agency, and corporate securities rated BBB- or better with maturities between 5 and 10 years. The index has a market value of over \$600 billion.

LEHMAN BROTHERS MUTUAL FUND LONG (10+) GOVERNMENT/CORPORATE INDEX -- is a market weighted index that contains individually priced U.S. Treasury, agency and corporate securities rated BBB- or better with maturities greater than 10 years. The index has a market value of over \$900 billion.

LIPPER SMALL COMPANY GROWTH FUND AVERAGE -- the average performance of small company growth funds as defined by Lipper Analytical Services, Inc. Lipper defines a small company growth fund as a fund that by prospectus or portfolio practice, limits its investments to companies on the basis of the size of the company. From time to time, Vanguard may advertise using the average performance and/or the average expense ratio of the small company growth funds. (This fund category was first established in 1982. For years prior to 1982, the results of the Lipper Small Company Growth category were estimated using the returns of the Funds that constituted the Group at its inception.)

RUSSELL 3000 INDEX -- consists of approximately the 3,000 largest stocks of U.S.-domiciled companies commonly traded on the New York and American Stock Exchanges or the NASDAQ over-the-counter market, accounting for over 90% of the market value of publicly traded Stocks in the U.S.

RUSSELL 2000 SMALL COMPANY STOCK INDEX -- consists of the smallest 2,000 stocks within the Russell 3000; a widely used benchmark for small capitalization common stocks.

LIPPER BALANCED FUND AVERAGE -- An industry benchmark of average balanced funds with similar investment objectives and policies, as measured by Lipper Analytical Services, Inc.

LIPPER NON-GOVERNMENT MONEY MARKET FUND AVERAGE -- An industry benchmark of average non-government money market funds with similar investment objectives and policies, as measured by Lipper Analytical Services, Inc.

LIPPER GOVERNMENT MONEY MARKET FUND AVERAGE -- An industry benchmark of average government money market funds with similar investment objectives and policies, as measured by Lipper Analytical Services, Inc.

FINANCIAL STATEMENTS

The Fund's Financial Statements for the year ended October 31, 1994, including the financial highlights for each of the five fiscal years in the period ended October 31, 1994, appearing in the Vanguard Explorer Fund 1994 Annual Report to Shareholders, and the report thereon of Price Waterhouse LLP, independent accountants, also appearing therein, are incorporated by reference in this Statement of Additional Information. The Fund's 1994 Annual Report to Shareholders is enclosed with this Statement of Additional Information.