Vanguard®

Annual Report | December 31, 2018

Vanguard Variable Insurance Fund

Diversified Value Portfolio

See the inside front cover for important information about access to your fund's annual and semiannual shareholder reports.

Important information about access to shareholder reports

Beginning on January 1, 2021, as permitted by regulations adopted by the Securities and Exchange Commission, paper copies of your fund's annual and semiannual shareholder reports will no longer be sent to you by mail, unless you specifically request them. Instead, you will be notified by mail each time a report is posted on the website and will be provided with a link to access the report.

If you have already elected to receive shareholder reports electronically, you will not be affected by this change and do not need to take any action. You may elect to receive shareholder reports and other communications from the fund electronically by contacting your financial intermediary (such as a broker-dealer or bank) or, if you invest directly with the fund, by calling Vanguard at one of the phone numbers on the back cover of this report or by logging on to vanguard.com.

You may elect to receive paper copies of all future shareholder reports free of charge. If you invest through a financial intermediary, you can contact the intermediary to request that you continue to receive paper copies. If you invest directly with the fund, you can call Vanguard at one of the phone numbers on the back cover of this report or log on to vanguard.com. Your election to receive paper copies will apply to all the funds you hold through an intermediary or directly with Vanguard.

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Please note: The opinions expressed in this report are just that—informed opinions. They should not be considered promises or advice. Also, please keep in mind that the information and opinions cover the period through the date on the front of this report. Of course, the risks of investing in your fund are spelled out in the prospectus.

CEO's Perspective

Tim Buckley
Chairman and Chief Executive Officer

Dear Planholder,

Over the years, I've found that prudent investors exhibit a common trait: discipline. No matter how the markets move or what new investing fad hits the headlines, those who stay focused on their goals and tune out the noise are set up for long-term success.

The prime gateway to investing is saving, and you don't usually become a saver without a healthy dose of discipline. Savers make the decision to sock away part of their income, which means spending less and delaying gratification, no matter how difficult that may be.

Of course, disciplined investing extends beyond diligent saving. The financial markets, in the short term especially, are unpredictable; I have yet to meet the investor who can time them perfectly. It takes discipline to resist the urge to go all-in when markets are frothy or to retreat when things look bleak.

Staying put with your investments is one strategy for handling volatility. Another, rebalancing, requires even more discipline because it means steering your money away from strong performers and toward poorer performers.

Patience—a form of discipline—is also the friend of long-term investors. Higher returns are the potential reward for weathering the market's turbulence and uncertainty.

It's important to be prepared for that turbulence, whenever it appears. Don't panic. Don't chase returns or look for answers outside the asset classes you trust. And be sure to rebalance periodically, even when there's turmoil.

Whether you're a master of self-control, get a boost from technology, or work with a professional advisor, know that discipline is necessary to get the most out of your investment portfolio. And know that Vanguard is with you for the entire ride.

Thank you for your continued loyalty.

Sincerely,

Mortimer J. Buckley
Chairman and Chief Executive Officer
January 17, 2019

Market Perspective

Stocks slide and volatility climbs

After a strong start, global stock markets fell, and volatility rose substantially at the end of the year. The spike in volatility resulted primarily from concerns over slowing global growth, rising U.S. interest rates, and heightened geopolitical uncertainty. These factors led to sharp declines across major equity markets for the 12-month period.

The CRSP US Total Market Index, the benchmark for Vanguard Total Stock Market Index Fund, returned –5.17% for the 12 months ended December 31, 2018. Seven of the fund's ten industry sectors declined, with only health care, utilities, and consumer services gaining ground. Financials and industrials were the sectors that detracted the most.

In the United States, technology stocks were hurt by concerns about slowing sales and high valuations. Manufacturers lost ground in part because of continued trade tensions between the United States and China. And stocks in the energy sector retreated amid declining oil prices.

Stocks outside the United States were also in negative territory. The U.K., for example, continued to be challenged by the Brexit negotiations. And European stocks lagged because of concerns about Italy's debt and Europe's economic dependence on emerging markets, which were hurt throughout much of the year by a rising dollar and trade protectionism.

Mixed results for bonds

Despite a solid macroeconomic backdrop throughout the year, bond markets also experienced bouts of volatility, as bond investors shared some of the same concerns that affected equity investors.

In the final quarter of the year, fixed income investors shied away from risky assets, including U.S. high-yield and investment-grade corporate bonds, which underperformed as credit spreads with U.S. Treasuries widened significantly. The impending partial shutdown of the U.S. government also weighed on investor sentiment and contributed to the relative strength of safe-haven assets as the year drew to a close.

For the year, the return for the bond market was essentially flat. The Bloomberg Barclays U.S. Aggregate Bond Index returned 0.01%. Bonds with shorter durations tended to perform the best. Mortgage-backed securities outperformed both U.S. Treasuries and corporate bonds for the year.

Treasury yields generally fell over the final quarter but finished the year higher. The yield of the 2-year Treasury note climbed 61 basis points to close the year at 2.49%. The yield of the 10-year Treasury increased 27 basis points to 2.68%.

The 12-month rise in yields was encouraged by the U.S. Federal Reserve. In December, the Fed lifted its target for short-term interest rates for the fourth time in 2018, to a range of 2.25%–2.5%. The central bank maintained that U.S. growth fundamentals and labor market conditions remain solid despite the recent market volatility, and lowered its long-term neutral target range to 2.75%–3%, signaling the likelihood for two more rate increases in 2019.

Bonds outside the United States, as measured by the Bloomberg Barclays Global Aggregate Index ex USD, returned –2.15% for the period. In general, higher-quality bonds with longer maturities tended to perform the best.

Market Barometer

	Average Annual Total Returns Periods Ended December 31, 2018		
	One Year	Three Years	Five Years
Stocks			
Russell 1000 Index (Large-caps)	-4.78%	9.09%	8.21%
Russell 2000 Index (Small-caps)	-11.01	7.36	4.41
Russell 3000 Index (Broad U.S. market)	-5.24	8.97	7.91
FTSE All-World ex US Index (International)	-14.13	4.58	1.05
Bonds			
Bloomberg Barclays U.S. Aggregate Bond Index (Broad taxable market)	0.01%	2.06%	2.52%
Bloomberg Barclays Municipal Bond Index (Broad tax-exempt market)	1.28	2.30	3.82
FTSE Three-Month U.S. Treasury Bill Index	1.86	0.98	0.59
CPI			
Consumer Price Index	1.91%	2.03%	1.51%

Diversified Value Portfolio

Advisor's Report

The Diversified Value Portfolio returned –9.12% for the 12 months ended December 31, 2018, behind the –8.27% return of its benchmark, the Russell 1000 Value Index. Please note that the returns for Vanguard Variable Insurance Fund are different from those of Vanguard Variable Annuity (and other plans that invest in the fund), which take into account insurance-related expenses.

The investment environment

What a difference a year makes. Volatility and rapid sentiment changes returned with a vengeance in 2018 as investors' appetite for risk changed dramatically. Although economic readings and earnings grew solidly for most of the year, worries increased about potential U.S. government policy errors. One major concern was that the Federal Reserve would tighten too much and too quickly in an increasingly fragile, late-cycle global economy. Another was the escalating trade wars, particularly with China, which weighed on many areas of the market.

As fears of a global slowdown intensified, the stocks being sold most aggressively encompassed many sectors (and broad swaths) of the market. This included companies leveraged to global trade and tariffs, particularly China, and those with interest rate or credit sensitivity. Unfortunately, this demarcation of risk encompasses so much of the economy and equity markets that it left virtually nowhere to hide.

Our successes and shortfalls

The portfolio experienced mixed results for the year. There were many successes that both highlighted and realized some of the value embedded in the portfolio, affirming our confidence in our long-term investment process. Unfortunately, these were offset by meaningful setbacks for some portfolio companies.

The largest shortfalls for performance were General Electric (GE), auto parts manufacturer Adient, and oil field services company Schlumberger, along with investments in the tobacco industry.

GE's power segment's operating income turned negative even though half of the business is stable and service-related. Also, certain liabilities related to the company's long-term-care business remain unknown. Its aviation and health care businesses continue to grow and are performing well. GE recently hired as CEO Larry Culp, former CEO of Danaher, who has an excellent track record for industrial turnarounds. He is expected to accelerate the power business restructuring and reduce balance sheet leverage. The planned monetization of the health care and transportation units and Baker Hughes (a GE company) will allow for deleveraging and reduced complexity. The stock, trading at $9 in mid-January 2019, is inexpensive based on an estimate of normalized earnings power of $1.

Adient underperformed because of operational challenges in its seat structures business, which resulted in significant losses, and worries about the automotive cycle. Operational difficulties have been exacerbated by a backlog of new launches that have resulted in significant complexity and strained resources. The Chinese auto market, which accounts for about half of Adient's net income, saw double-digit declines during the fourth quarter. We conclude that these challenges will continue for some time, and we are evaluating the investment.

Schlumberger performed poorly after negative earnings revisions as oil price declines caused more uncertainty. Although international markets are progressing, the U.S. land market continued to weaken. Schlumberger has leading-edge technology, and though it may take some time, the company will benefit greatly when global oil field services recover.

Lastly, tobacco shares fell after the Food and Drug Administration announced a push to regulate nicotine levels and ban menthol in cigarettes. Noncombustible products also added to concerns. As a result, the consumer staples sector was the largest drag on performance for the year. Tobacco companies are approaching the changes in different ways, which could affect how they allocate capital. Altria Group's recent large equity investment in Juul is a prime example. We are evaluating what this deal might mean for capital allocation. Tobacco industry shares are trading at meaningful discounts to the market, with a dividend yield of 7% on average, well above market levels.

Although these challenges were disappointing, we were encouraged by instances where our investment process worked well. Two portfolio companies were acquired for premiums and added to performance: Twenty-First Century Fox Class A and Express Scripts. We bought Twenty-First Century Fox when media companies, in general, were being sold over market disruption concerns as consumers increasingly switched to online streaming content. Disney later realized the stock's value in a deal that was nearly double the price we had paid. Express Scripts was purchased by Cigna, leading to a gain that made our health care sector the largest contributor to performance.

Holdings in retailers Lowe's and Dollar General were other examples of how our investment process takes advantage of market disruption opportunities. We bought these companies when the industry was under severe pressure because of concerns about mounting competition from online retailers, primarily Amazon. At the time, we believed that these were babies being thrown out with the bathwater. These investments were a large boost to performance as market participants realized that the “Amazon” impact to these companies would be limited, and fundamental outlooks remained steady or improved.

Lastly, Microsoft continued to perform well. The results are another example of how our long-term investment horizon works in our favor. We bought Microsoft years ago at a steep discount when market participants were worried about the consumer PC business, which then represented a paltry 20% of sales. We took a longer-term view, realizing that they were missing the boat on the corporate business services side that would drive the business. Today, Microsoft is one of the leaders in cloud architecture, which is growing rapidly and has led the company to be one of the largest contributors to performance.

Our portfolio positioning

The current cycle of growth-stock dominance has been the longest in 90 years, producing one of the strongest cycles ever recorded. Value has been out of favor for what seems like an eternity, with increasing calls for its demise. However, history shows repeated shifts between growth and value leadership, and when leadership does shift, value typically outperforms meaningfully for many years. We remain committed to the value discipline, buying a concentrated portfolio of good companies trading at valuations below the broad market for reasons that we believe to be temporary or overblown.

We want to emphasize our steadfast commitment to value, as some market participants in the value space seem to be stretching to buy growth companies using logic that is inconsistent with our definition of value. In prior cycles, such as during the tech bubble of the late 1990s, we saw similar justifications by some managers, with unfortunate outcomes for many of their investors. Thank you for your continued confidence and investment.

Portfolio Managers:

Jeff Fahrenbruch, Managing Director

David Ganucheau, Managing Director

Barrow, Hanley, Mewhinney & Strauss, LLC

January 17, 2019

About Your Portfolio's Expenses

As a shareholder of the portfolio, you incur ongoing costs, which include costs for portfolio management, administrative services, and shareholder reports (like this one), among others. Operating expenses, which are deducted from a portfolio's gross income, directly reduce the investment return of the portfolio.

A portfolio's expenses are expressed as a percentage of its average net assets. This figure is known as the expense ratio. The following examples are intended to help you understand the ongoing costs (in dollars) of investing in your portfolio and to compare these costs with those of other mutual funds. The examples are based on an investment of $1,000 made at the beginning of the period shown and held for the entire period.

The table below illustrates your portfolio's costs in two ways:

• **Based on actual portfolio return.** This section helps you to estimate the actual expenses that you paid over the period. The "Ending Account Value" shown is derived from the portfolio's actual return, and the third column shows the dollar amount that would have been paid by an investor who started with $1,000 in the portfolio. You may use the information here, together with the amount you invested, to estimate the expenses that you paid over the period.

To do so, simply divide your account value by $1,000 (for example, an $8,600 account value divided by $1,000 = 8.6), then multiply the result by the number given for your portfolio under the heading "Expenses Paid During Period."

• **Based on hypothetical 5% yearly return.** This section is intended to help you compare your portfolio's costs with those of other mutual funds. It assumes that the portfolio had a yearly return of 5% before expenses, but that the expense ratio is unchanged. In this case—because the return used is not the portfolio's actual return—the results do not apply to your investment. The example is useful in making comparisons because the Securities and Exchange Commission requires all mutual funds to calculate expenses based on a 5% return. You can assess your portfolio's costs by comparing this hypothetical example with the hypothetical examples that appear in shareholder reports of other funds.

Note that the expenses shown in the table are meant to highlight and help you compare *ongoing* costs only and do not reflect transaction costs incurred by the portfolio for buying and selling securities. The portfolio's expense ratio does not reflect additional fees and expenses associated with the annuity or life insurance program through which you invest.

The calculations assume no shares were bought or sold during the period. Your actual costs may have been higher or lower, depending on the amount of your investment and the timing of any purchases or redemptions.

You can find more information about the portfolio's expenses in the Financial Statements section. For additional information on operating expenses and other shareholder costs, please refer to the prospectus.

Six Months Ended December 31, 2018

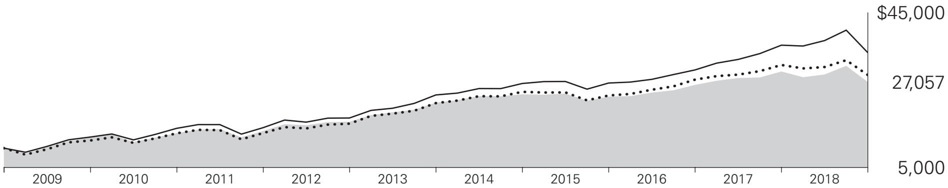
Diversified Value Portfolio	Beginning Account Value 6/30/2018	Ending Account Value 12/31/2018	Expenses Paid During Period[1]
Based on Actual Portfolio Return	$1,000.00	$932.94	$1.17
Based on Hypothetical 5% Yearly Return	1,000.00	1,024.00	1.22

1 The calculations are based on expenses incurred in the most recent six-month period. The portfolio's annualized six-month expense ratio for that period is 0.24%. The dollar amounts shown as "Expenses Paid" are equal to the annualized expense ratio multiplied by the average account value over the period, multiplied by the number of days in the most recent six-month period, then divided by the number of days in the most recent 12-month period (184/365).

Performance Summary

All of the returns in this report represent past performance, which is not a guarantee of future results that may be achieved by the portfolio. (Current performance may be lower or higher than the performance data cited. For performance data current to the most recent month-end, visit our website at vanguard.com/performance.) Note, too, that both investment returns and principal value can fluctuate widely, so an investor's shares, when sold, could be worth more or less than their original cost. The returns shown do not reflect taxes that a shareholder would pay on portfolio distributions or on the sale of portfolio shares. Nor do the returns reflect fees and expenses associated with the annuity or life insurance program through which a shareholder invests. If these fees and expenses were included, the portfolio's returns would be lower.

Cumulative Performance: December 31, 2008–December 31, 2018
Initial Investment of $10,000



	Average Annual Total Returns Periods Ended December 31, 2018 One Year	Five Years	Ten Years	Final Value of a $10,000 Investment
Diversified Value Portfolio	-9.12%	4.47%	10.47%	$27,057
Russell 1000 Value Index	-8.27	5.95	11.18	28,853
Dow Jones U.S. Total Stock Market Float Adjusted Index	-5.30	7.86	13.22	34,625

See Financial Highlights for dividend and capital gains information.

Sector Diversification

As of December 31, 2018

Communication Services	5.6%
Consumer Discretionary	7.7
Consumer Staples	6.9
Energy	12.3
Financials	17.9
Health Care	19.2
Industrials	9.5
Information Technology	10.1
Materials	6.8
Real Estate	0.0
Utilities	4.0

The table reflects the portfolio's equity exposure, based on its investments in stocks and stock index futures. Any holdings in short-term reserves are excluded. Sector categories are based on the Global Industry Classification Standard ("GICS"), except for the "Other" category (if applicable), which includes securities that have not been provided a GICS classification as of the effective reporting period.

Financial Statements

Statement of Net Assets

As of December 31, 2018

The portfolio reports a complete list of its holdings in regulatory filings four times in each fiscal year, at the quarter-ends. For the second and fourth fiscal quarters, the lists appear in the portfolio's semiannual and annual reports to shareholders. For the first and third fiscal quarters, the portfolio files the lists with the Securities and Exchange Commission on Form N-Q. Shareholders can look up the portfolio's Forms N-Q on the SEC's website at sec.gov.

		Shares	Market Value• ($000)
Common Stocks (97.4%)			
Communication Services (5.4%)			
	Comcast Corp. Class A	869,970	29,622
	Verizon Communications Inc.	206,609	11,616
	AT&T Inc.	246,882	7,046
			48,284
Consumer Discretionary (7.5%)			
	Dollar General Corp.	306,878	33,167
	Lowe's Cos. Inc.	336,583	31,087
	Adient plc	125,465	1,890
			66,144
Consumer Staples (6.7%)			
	Philip Morris International Inc.	335,906	22,425
	Imperial Brands plc ADR	639,220	19,509
	Altria Group Inc.	350,124	17,293
			59,227
Energy (12.0%)			
	Phillips 66	249,777	21,518
	Occidental Petroleum Corp.	344,470	21,144
	ConocoPhillips	308,786	19,253
	BP plc ADR	477,416	18,104
	Schlumberger Ltd.	452,285	16,318
	Chevron Corp.	93,537	10,176
			106,513
Financials (17.4%)			
	Wells Fargo & Co.	635,101	29,265
	American Express Co.	294,024	28,026
	US Bancorp	609,510	27,855
	JPMorgan Chase & Co.	231,308	22,580
	American International Group Inc.	495,116	19,512
	Bank of New York Mellon Corp.	398,949	18,779
	Navient Corp.	490,028	4,317
*	SLM Corp.	490,213	4,074
			154,408
Health Care (18.7%)			
	Pfizer Inc.	749,091	32,698
	Johnson & Johnson	211,884	27,344
	Medtronic plc	293,513	26,698
	Sanofi ADR	578,837	25,127
	CVS Health Corp.	371,135	24,317
*	Cigna Corp.	97,271	18,474
	Cardinal Health Inc.	261,672	11,670
			166,328
Industrials (9.3%)			
	United Technologies Corp.	273,709	29,144
	Johnson Controls International plc	863,702	25,609
	General Electric Co.	1,901,880	14,397
	General Dynamics Corp.	83,423	13,115
			82,265
Information Technology (9.8%)			
	Oracle Corp.	706,424	31,895
	QUALCOMM Inc.	529,028	30,107
	Microsoft Corp.	248,514	25,242
			87,244
Materials (6.7%)			
	Air Products & Chemicals Inc.	211,121	33,790
	DowDuPont Inc.	473,161	25,304
			59,094
Utilities (3.9%)			
	Dominion Energy Inc.	306,705	21,917
	Exelon Corp.	284,160	12,816
			34,733
Total Common Stocks (Cost $869,387)			864,240
Temporary Cash Investment (2.5%)			
Money Market Fund (2.5%)			
1	Vanguard Market Liquidity Fund, 2.530% (Cost $22,032)	220,318	22,032
Total Investments (99.9%) (Cost $891,419)			886,272

	Amount ($000)
Other Assets and Liabilities (0.1%)	
Other Assets	
Investment in Vanguard	52
Receivables for Investment Securities Sold	342
Receivables for Accrued Income	2,859
Receivables for Capital Shares Issued	668
Total Other Assets	3,921
Liabilities	
Payables for Investment Securities Purchased	(14)
Payables for Capital Shares Redeemed	(1,423)
Payables to Investment Advisor	(220)
Payables to Vanguard	(1,144)
Total Liabilities	(2,801)
Net Assets (100%)	
Applicable to 61,908,726 outstanding $.001 par value shares of beneficial interest (unlimited authorization)	887,392
Net Asset Value Per Share	$14.33

At December 31, 2018, net assets consisted of:

	Amount ($000)
Paid-in Capital	812,299
Total Distributable Earnings (Loss)	75,093
Net Assets	887,392

• See Note A in Notes to Financial Statements.

* Non-income-producing security.

1 Affiliated money market fund available only to Vanguard funds and certain trusts and accounts managed by Vanguard. Rate shown is the 7-day yield.

ADR—American Depositary Receipt.

See accompanying Notes, which are an integral part of the Financial Statements.

Statement of Operations

	Year Ended December 31, 2018 ($000)
Investment Income	
Income	
Dividends[1]	29,558
Interest[2]	220
Securities Lending—Net	14
Total Income	29,792
Expenses	
Investment Advisory Fees—Note B	
Basic Fee	1,314
Performance Adjustment	(342)
The Vanguard Group—Note C	
Management and Administrative	1,491
Marketing and Distribution	140
Custodian Fees	9
Auditing Fees	31
Shareholders' Reports	14
Trustees' Fees and Expenses	1
Total Expenses	2,658
Expenses Paid Indirectly	(16)
Net Expenses	2,642
Net Investment Income	**27,150**
Realized Net Gain (Loss) on Investment Securities Sold[2]	**54,769**
Change in Unrealized Appreciation (Depreciation) of Investment Securities[2]	**(172,551)**
Net Increase (Decrease) in Net Assets Resulting from Operations	**(90,632)**

1 Dividends are net of foreign withholding taxes of $161,000.

2 Interest income, realized net gain (loss), and change in unrealized appreciation (depreciation) from an affiliated company of the portfolio were $219,000, ($5,000), and $0, respectively. Purchases and sales are for temporary cash investment purposes.

Statement of Changes in Net Assets

	Year Ended December 31, 2018 ($000)	2017 ($000)
Increase (Decrease) in Net Assets		
Operations		
Net Investment Income	27,150	27,806
Realized Net Gain (Loss)	54,769	54,302
Change in Unrealized Appreciation (Depreciation)	(172,551)	58,076
Net Increase (Decrease) in Net Assets Resulting from Operations	(90,632)	140,184
Distributions		
Net Investment Income	(27,747)	(31,847)
Realized Capital Gain[1]	(54,228)	(106,243)
Total Distributions	(81,975)	(138,090)
Capital Share Transactions		
Issued	95,428	83,423
Issued in Lieu of Cash Distributions	81,975	138,090
Redeemed	(254,507)	(216,526)
Net Increase (Decrease) from Capital Share Transactions	(77,104)	4,987
Total Increase (Decrease)	(249,711)	7,081
Net Assets		
Beginning of Period	**1,137,103**	**1,130,022**
End of Period	**887,392**	**1,137,103**

1 Includes fiscal 2018 and 2017 short-term gain distributions totaling $420,000 and $14,464,000. Short-term gain distributions are treated as ordinary income dividends for tax purposes.

Financial Highlights

For a Share Outstanding Throughout Each Period	Year Ended December 31, 2018	2017	2016	2015	2014
Net Asset Value, Beginning of Period	**$17.04**	**$17.11**	**$16.55**	**$18.65**	**$18.10**
Investment Operations					
Net Investment Income	.412[1]	.401[1]	.496	.471	.447
Net Realized and Unrealized Gain (Loss) on Investments	(1.872)	1.658	1.468	(.901)	1.248
Total from Investment Operations	(1.460)	2.059	1.964	(.430)	1.695
Distributions					
Dividends from Net Investment Income	(.423)	(.491)	(.461)	(.466)	(.415)
Distributions from Realized Capital Gains	(.827)	(1.638)	(.943)	(1.204)	(.730)
Total Distributions	(1.250)	(2.129)	(1.404)	(1.670)	(1.145)
Net Asset Value, End of Period	**$14.33**	**$17.04**	**$17.11**	**$16.55**	**$18.65**
Total Return	**-9.12%**	**13.16%**	**12.96%**	**-2.45%**	**9.83%**
Ratios/Supplemental Data					
Net Assets, End of Period (Millions)	$887	$1,137	$1,130	$1,060	$1,213
Ratio of Total Expenses to Average Net Assets[2]	0.25%	0.27%	0.27%	0.28%	0.34%
Ratio of Net Investment Income to Average Net Assets	2.58%	2.45%	3.01%	2.55%	2.50%
Portfolio Turnover Rate	18%	18%	34%	13%	16%

1 Calculated based on average shares outstanding.

2 Includes performance-based investment advisory fee increases (decreases) of (0.03%), (0.03%), (0.03%), (0.03%), and (0.01%).

Notes to Financial Statements

Diversified Value Portfolio, a portfolio of Vanguard Variable Insurance Funds, is registered under the Investment Company Act of 1940 as an open-end investment company. The portfolio's shares are only available for purchase by separate accounts of insurance companies as investments for variable annuity plans, variable life insurance contracts, or other variable benefit insurance contracts.

A. The following significant accounting policies conform to generally accepted accounting principles for U.S. investment companies. The portfolio consistently follows such policies in preparing its financial statements.

1. Security Valuation: Securities are valued as of the close of trading on the New York Stock Exchange (generally 4 p.m., Eastern time) on the valuation date. Equity securities are valued at the latest quoted sales prices or official closing prices taken from the primary market in which each security trades; such securities not traded on the valuation date are valued at the mean of the latest quoted bid and asked prices. Securities for which market quotations are not readily available, or whose values have been materially affected by events occurring before the portfolio's pricing time but after the close of the securities' primary markets, are valued by methods deemed by the board of trustees to represent fair value. Investments in Vanguard Market Liquidity Fund are valued at that fund's net asset value.

2. Federal Income Taxes: The portfolio intends to continue to qualify as a regulated investment company and distribute all of its taxable income. Management has analyzed the portfolio's tax positions taken for all open federal income tax years (December 31, 2015–2018), and has concluded that no provision for federal income tax is required in the portfolio's financial statements.

3. Distributions: Distributions to shareholders are recorded on the ex-dividend date. Distributions are determined on a tax basis and may differ from net investment income and realized capital gains for financial reporting purposes.

4. Securities Lending: To earn additional income, the portfolio lends its securities to qualified institutional borrowers. Security loans are subject to termination by the portfolio at any time, and are required to be secured at all times by collateral in an amount at least equal to the market value of securities loaned.

Daily market fluctuations could cause the value of loaned securities to be more or less than the value of the collateral received. When this occurs, the collateral is adjusted and settled before the opening of the market on the next business day. The portfolio further mitigates its counterparty risk by entering into securities lending transactions only with a diverse group of prequalified counterparties, monitoring their financial strength, and entering into master securities lending agreements with its counterparties. The master securities lending agreements provide that, in the event of a counterparty's default (including bankruptcy), the portfolio may terminate any loans with that borrower, determine the net amount owed, and sell or retain the collateral up to the net amount owed to the portfolio; however, such actions may be subject to legal proceedings. While collateral mitigates counterparty risk, in the event of a default, the portfolio may experience delays and costs in recovering the securities loaned. The portfolio invests cash collateral received in Vanguard Market Liquidity Fund, and records a liability in the Statement of Net Assets for the return of the collateral, during the period the securities are on loan. Securities lending income represents fees charged to borrowers plus income earned on invested cash collateral, less expenses associated with the loan. During the term of the loan, the portfolio is entitled to all distributions made on or in respect of the loaned securities.

5. Credit Facility: The portfolio and certain other funds managed by The Vanguard Group ("Vanguard") participate in a $3.1 billion committed credit facility provided by a syndicate of lenders pursuant to a credit agreement that may be renewed annually; each fund is individually liable for its borrowings, if any, under the credit facility. Borrowings may be utilized for temporary and emergency purposes, and are subject to the portfolio's regulatory and contractual borrowing restrictions. The participating funds are charged administrative fees and an annual commitment fee of 0.10% of the undrawn amount of the facility; these fees are allocated to the funds based on a method approved by the portfolio's board of trustees and included in Management and Administrative expenses on the portfolio's Statement of Operations. Any borrowings under this facility bear interest at a rate based upon the higher of the one-month London Interbank Offered Rate, federal funds effective rate, or overnight bank funding rate plus an agreed-upon spread.

The portfolio had no borrowings outstanding at December 31, 2018, or at any time during the period then ended.

6. Other: Dividend income is recorded on the ex-dividend date. Interest income includes income distributions received from Vanguard Market Liquidity Fund and is accrued daily. Security transactions are accounted for on the date securities are bought or sold. Costs used to determine realized gains (losses) on the sale of investment securities are those of the specific securities sold.

B. Barrow, Hanley, Mewhinney & Strauss, LLC, provides investment advisory services to the portfolio for a fee calculated at an annual percentage rate of average net assets. The basic fee is subject to quarterly adjustments based on the portfolio's performance relative to the MSCI Prime Market 750 Index for the preceding three years. For the year ended December 31, 2018, the investment advisory fee represented an effective annual basic rate of 0.13% of the portfolio's average net assets before a decrease of $342,000 (0.03%) based on performance.

C. In accordance with the terms of a Funds' Service Agreement (the "FSA") between Vanguard and the portfolio, Vanguard furnishes to the portfolio corporate management, administrative, marketing, and distribution services at Vanguard's cost of operations (as defined by the FSA). These costs of operations are allocated to the portfolio based on methods and guidelines approved by the board of trustees. Vanguard does not require reimbursement in the current period for certain costs of operations (such as deferred compensation/benefits and risk/insurance costs); the portfolio's liability for these costs of operations is included in Payables to Vanguard on the Statement of Net Assets. All other costs of operations payable to Vanguard are generally settled twice a month.

Upon the request of Vanguard, the portfolio may invest up to 0.40% of its net assets as capital in Vanguard. At December 31, 2018, the portfolio had contributed to Vanguard capital in the amount of $52,000, representing 0.01% of the portfolio's net assets and 0.02% of Vanguard's capitalization. The portfolio's trustees and officers are also directors and employees, respectively, of Vanguard.

D. The portfolio has asked its investment advisor to direct certain security trades, subject to obtaining the best price and execution, to brokers who have agreed to rebate to the portfolio part of the commissions generated. Such rebates are used solely to reduce the portfolio's management and administrative expenses. For the year ended December 31, 2018, these arrangements reduced the portfolio's expenses by $16,000 (an annual rate of 0.00% of average net assets).

E. Various inputs may be used to determine the value of the portfolio's investments. These inputs are summarized in three broad levels for financial statement purposes. The inputs or methodologies used to value securities are not necessarily an indication of the risk associated with investing in those securities.

Level 1—Quoted prices in active markets for identical securities.
Level 2—Other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, credit risk, etc.).
Level 3—Significant unobservable inputs (including the portfolio's own assumptions used to determine the fair value of investments). Any investments valued with significant unobservable inputs are noted on the Statement of Net Assets.

At December 31, 2018, 100% of the market value of the portfolio's investments was determined based on Level 1 inputs.

F. Permanent differences between book-basis and tax-basis components of net assets, if any, are reclassified among capital accounts in the financial statements to reflect their tax character. These reclassifications have no effect on net assets or net asset value per share.

Temporary differences between book-basis and tax-basis components of total distributable earnings (loss) arise when certain items of income, gain, or loss are recognized in different periods for financial statement and tax purposes; these differences will reverse at some time in the future. The differences are primarily related to the tax deferral of losses on wash sales. As of period end, the tax-basis components of total distributable earnings (loss) are detailed in the table as follows:

	Amount ($000)
Undistributed Ordinary Income	28,378
Undistributed Long-Term Gains	52,944
Capital Loss Carryforwards (Non-expiring)	—
Net Unrealized Gains (Losses)	(5,147)

As of December 31, 2018, gross unrealized appreciation and depreciation for investments based on cost for U.S. federal income tax purposes were as follows:

	Amount ($000)
Tax Cost	891,419
Gross Unrealized Appreciation	135,485
Gross Unrealized Depreciation	(140,632)
Net Unrealized Appreciation (Depreciation)	(5,147)

G. During the year ended December 31, 2018, the portfolio purchased $189,393,000 of investment securities and sold $339,396,000 of investment securities, other than temporary cash investments.

H. Capital shares issued and redeemed were:

	Year Ended December 31,	
	2018 Shares (000)	2017 Shares (000)
Issued	5,928	5,070
Issued in Lieu of Cash Distributions	5,292	8,835
Redeemed	(16,026)	(13,222)
Net Increase (Decrease) in Shares Outstanding	(4,806)	683

At December 31, 2018, two shareholders were each a record or beneficial owner of 25% or more of the portfolio's net assets, with a combined ownership of 68%. If one of these shareholders were to redeem its investment in the portfolio, the redemption might result in an increase in the portfolio's expense ratio or cause the portfolio to incur higher transaction costs.

I. Management has determined that no events or transactions occurred subsequent to December 31, 2018, that would require recognition or disclosure in these financial statements.

Report of Independent Registered Public Accounting Firm

To the Board of Trustees of Vanguard Variable Insurance Funds and Shareholders of Diversified Value Portfolio

Opinion on the Financial Statements

We have audited the accompanying statement of net assets of Diversified Value Portfolio (one of the portfolios constituting Vanguard Variable Insurance Funds, referred to hereafter as the "Portfolio") as of December 31, 2018, the related statement of operations for the year ended December 31, 2018, the statement of changes in net assets for each of the two years in the period ended December 31, 2018, including the related notes, and the financial highlights for each of the five years in the period ended December 31, 2018 (collectively referred to as the "financial statements"). In our opinion, the financial statements present fairly, in all material respects, the financial position of the Portfolio as of December 31, 2018, the results of its operations for the year then ended, the changes in its net assets for each of the two years in the period ended December 31, 2018 and the financial highlights for each of the five years in the period ended December 31, 2018 in conformity with accounting principles generally accepted in the United States of America.

Basis for Opinion

These financial statements are the responsibility of the Portfolio's management. Our responsibility is to express an opinion on the Portfolio's financial statements based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) ("PCAOB") and are required to be independent with respect to the Portfolio in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits of these financial statements in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud.

Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. Our procedures included confirmation of securities owned as of December 31, 2018 by correspondence with the custodian, transfer agent, and brokers; when replies were not received from brokers, we performed other auditing procedures. We believe that our audits provide a reasonable basis for our opinion.

/s/PricewaterhouseCoopers LLP
Philadelphia, Pennsylvania
February 13, 2019

We have served as the auditor of one or more investment companies in The Vanguard Group of Funds since 1975.

Special 2018 tax information (unaudited) for corporate shareholders only for Diversified Value Portfolio, a portfolio of Vanguard Variable Insurance Funds

This information for the fiscal year ended December 31, 2018, is included pursuant to provisions of the Internal Revenue Code for corporate shareholders only.

The portfolio distributed $53,808,000 as capital gain dividends (20% rate gain distributions) to shareholders during the fiscal year.

For corporate shareholders, 90.2% of investment income (dividend income plus short-term gains, if any) qualifies for the dividends-received deduction.

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The People Who Govern Your Fund

The trustees of your mutual fund are there to see that the fund is operated and managed in your best interests since, as a shareholder, you are a part owner of the fund. Your fund's trustees also serve on the board of directors of The Vanguard Group, Inc., which is owned by the Vanguard funds and provides services to them.

A majority of Vanguard's board members are independent, meaning that they have no affiliation with Vanguard or the funds they oversee, apart from the sizable personal investments they have made as private individuals. The independent board members have distinguished backgrounds in business, academia, and public service. Each of the trustees and executive officers oversees 212 Vanguard funds.

Information for each trustee and executive officer of the fund appears below. The mailing address of the trustees and officers is P.O. Box 876, Valley Forge, PA 19482. More information about the trustees is in the *Statement of Additional Information*, which can be obtained, without charge, by contacting Vanguard at 800-662-7447, or online at vanguard.com.

1 Mr. McNabb and Mr. Buckley are considered "interested persons," as defined in the Investment Company Act of 1940, because they are officers of the Vanguard funds.

P.O. Box 2600
Valley Forge, PA 19482-2600

Connect with Vanguard® > vanguard.com

Fund Information > 800-662-7447

Annuity and Insurance Services > 800-522-5555

Institutional Investor Services > 800-523-1036

Text Telephone for People Who Are Deaf or Hard of Hearing > 800-749-7273

This material may be used in conjunction with the offering of shares of any Vanguard fund only if preceded or accompanied by the fund's current prospectus.

You can obtain a free copy of Vanguard's proxy voting guidelines by visiting vanguard.com/proxyreporting or by calling Vanguard at 800-662-2739. The guidelines are also available from the SEC's website, sec.gov. In addition, you may obtain a free report on how your fund voted the proxies for securities it owned during the 12 months ended June 30. To get the report, visit either vanguard.com/proxyreporting or sec.gov.

All comparative mutual fund data are from Lipper, a Thomson Reuters Company, or Morningstar, Inc., unless otherwise noted.

You can review information about your portfolio on the SEC's website, and you can receive copies of this information, for a fee, by sending a request via email addressed to publicinfo@sec.gov.

The funds or securities referred to herein that are offered by The Vanguard Group and track an MSCI index are not sponsored, endorsed, or promoted by MSCI, and MSCI bears no liability with respect to any such funds or securities. For such funds or securities, the prospectus or the *Statement of Additional Information* contains a more detailed description of the limited relationship MSCI has with The Vanguard Group.

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