



Semiannual Report | June 30, 2019

Vanguard Variable Insurance Fund

Real Estate Index 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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Real Estate Index Portfolio

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 accompanying table 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 June 30, 2019

	Beginning Account Value 12/31/2018	Ending Account Value 6/30/2019	Expenses Paid During Period
Real Estate Index Portfolio			
Based on Actual Portfolio Return	\$1,000.00	\$1,192.44	\$1.41
Based on Hypothetical 5% Yearly Return	1,000.00	1,023.51	1.30

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 0.26%. 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 (181/365).

Subindustry Diversification

As of June 30, 2019

Diversified REITs	4.9%
Health Care REITs	9.6
Hotel & Resort REITs	4.5
Industrial REITs	7.8
Office REITs	9.3
Residential REITs	14.4
Retail REITs	12.9
Specialized REITs	33.1
Real Estate Management and Development	3.5

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.

The Global Industry Classification Standard ("GICS") was developed by and is the exclusive property and a service mark of MSCI Inc. ("MSCI") and Standard and Poor's, a division of McGraw-Hill Companies, Inc. ("S&P"), and is licensed for use by Vanguard. Neither MSCI, S&P nor any third party involved in making or compiling the GICS or any GICS classification makes any express or implied warranties or representations with respect to such standard or classification (or the results to be obtained by the use thereof), and all such parties hereby expressly disclaim all warranties of originality, accuracy, completeness, merchantability or fitness for a particular purpose with respect to any such standard or classification. Without limiting any of the foregoing, in no event shall MSCI, S&P, any of its affiliates or any third party involved in making or compiling the GICS or any GICS classification have any liability for any direct, indirect, special, punitive, consequential or any other damages (including lost profits) even if notified of the possibility of such damages.

Financial Statements (unaudited)

Statement of Net Assets

As of June 30, 2019

The portfolio files its complete schedule of portfolio holdings with the Securities and Exchange Commission (SEC) for the first and third quarters of each fiscal year as an exhibit to its reports on Form N-PORT. The portfolio's Form N-PORT reports are available on the SEC's website at www.sec.gov.

	Shares	Market Value* (\$000)		Shares	Market Value* (\$000)		Shares	Market Value* (\$000)
Equity Real Estate Investment Trusts (REITs) (96.3%)¹			Apple Hospitality REIT Inc.			Corporate Office Properties Trust		
Diversified REITs (4.9%)			Sunstone Hotel Investors Inc.			Paramount Group Inc.		
WP Carey Inc.	161,230	13,089	RLJ Lodging Trust			Brandywine Realty Trust		
VEREIT Inc.	942,282	8,490	MGM Growth Properties LLC Class A			Piedmont Office Realty Trust Inc. Class A		
Liberty Property Trust	143,645	7,188	Xenia Hotels & Resorts Inc.			Columbia Property Trust Inc.		
STORE Capital Corp.	197,296	6,548	DiamondRock Hospitality Co.			Mack-Cali Realty Corp.		
PS Business Parks Inc.	19,981	3,367	Chesapeake Lodging Trust			Office Properties Income Trust		
Colony Capital Inc.	452,194	2,261	Summit Hotel Properties Inc.			Easterly Government Properties Inc.		
American Assets Trust Inc.	47,447	2,236	Chatham Lodging Trust			Franklin Street Properties Corp.		
Empire State Realty Trust Inc.	143,713	2,128	Hersha Hospitality Trust Class A			NorthStar Realty Europe Corp.		
Washington REIT	77,355	2,068	CorePoint Lodging Inc.			City Office REIT Inc.		
Lexington Realty Trust	204,639	1,926	Ashford Hospitality Trust Inc.					
Global Net Lease Inc.	81,149	1,592	Braemar Hotels & Resorts Inc.					
Alexander & Baldwin Inc.	66,218	1,530						
Essential Properties Realty Trust Inc.	46,133	924	Industrial REITs (7.9%)			Residential REITs (14.3%)		
iStar Inc.	65,453	813	Prologis Inc.			AvalonBay Communities Inc.		
Armada Hoffer Properties Inc.	48,089	796	Duke Realty Corp.			Equity Residential		
Gladstone Commercial Corp.	28,273	600	Americold Realty Trust			Essex Property Trust Inc.		
One Liberty Properties Inc.	13,817	400	First Industrial Realty Trust Inc.			Mid-America Apartment Communities Inc.		
Winthrop Realty Trust	32,397	35	EastGroup Properties Inc.			UDR Inc.		
		55,991	Rexford Industrial Realty Inc.			Invitation Homes Inc.		
			STAG Industrial Inc.			Sun Communities Inc.		
Health Care REITs (9.6%)			Terreno Realty Corp.			Equity LifeStyle Properties Inc.		
Welltower Inc.	375,948	30,651	Hannon Armstrong Sustainable Infrastructure Capital Inc.			Camden Property Trust		
Ventas Inc.	346,759	23,701	Industrial Logistics Properties Trust			Apartment Investment & Management Co.		
HCP Inc.	464,525	14,856	Monmouth Real Estate Investment Corp.			American Homes 4 Rent Class A		
Omega Healthcare Investors Inc.	209,339	7,693	Innovative Industrial Properties Inc.			American Campus Communities Inc.		
Medical Properties Trust Inc.	360,768	6,292				Independence Realty Trust Inc.		
Healthcare Trust of America Inc. Class A	199,891	5,483	Office REITs (9.3%)			NexPoint Residential Trust Inc.		
Healthcare Realty Trust Inc.	122,163	3,826	Boston Properties Inc.			Investors Real Estate Trust Preferred Apartment Communities Inc. Class A		
Sabra Health Care REIT Inc.	174,338	3,433	Alexandria Real Estate Equities Inc.			Front Yard Residential Corp.		
National Health Investors Inc.	41,826	3,264	Vornado Realty Trust			UMH Properties Inc.		
Physicians Realty Trust	178,597	3,115	Kilroy Realty Corp.					
CareTrust REIT Inc.	87,216	2,074	SL Green Realty Corp.					
Senior Housing Properties Trust	230,719	1,908	Douglas Emmett Inc.					
LTC Properties Inc.	38,376	1,752	Cousins Properties Inc.					
Universal Health Realty Income Trust	12,708	1,079	Hudson Pacific Properties Inc.					
Community Healthcare Trust Inc.	17,353	684	JBG SMITH Properties					
New Senior Investment Group Inc.	80,535	541	Highwoods Properties Inc.					
		110,352	Equity Commonwealth					
Hotel & Resort REITs (4.5%)						Retail REITs (12.8%)		
Host Hotels & Resorts Inc.	720,313	13,124				Simon Property Group Inc.		
Park Hotels & Resorts Inc.	196,696	5,421				Realty Income Corp.		
Hospitality Properties Trust	160,703	4,017				Regency Centers Corp.		
Ryman Hospitality Properties Inc.	47,541	3,855				Federal Realty Investment Trust		
Pebblebrook Hotel Trust	127,079	3,581				National Retail Properties Inc.		
						Kimco Realty Corp.		
						Brixmor Property Group Inc.		

Derivative Financial Instruments Outstanding as of Period End

Futures Contracts

				(\$000)
	Expiration	Number of Long (Short) Contracts	Notional Amount	Value and Unrealized Appreciation (Depreciation)
Long Futures Contracts				
Dow Jones U.S. Real Estate Index	September 2019	65	2,251	(36)

Statement of Operations

	Six Months Ended June 30, 2019
	(\$000)
Investment Income	
Income	
Dividends	17,483
Interest ¹	17
Securities Lending—Net	24
Total Income	17,524
Expenses	
The Vanguard Group—Note B	
Investment Advisory Services	134
Management and Administrative	1,217
Marketing and Distribution	48
Custodian Fees	12
Shareholders' Reports	7
Trustees' Fees and Expenses	—
Total Expenses	1,418
Net Investment Income	16,106
Realized Net Gain (Loss)	
Investment Securities Sold ¹	2,860
Futures Contracts	237
Capital Gain Distributions Received	2,164
Realized Net Gain (Loss)	5,261
Change in Unrealized Appreciation (Depreciation)	
Investment Securities ¹	163,827
Futures Contracts	97
Change in Unrealized Appreciation (Depreciation)	163,924
Net Increase (Decrease) in Net Assets Resulting from Operations	185,291

¹ Interest income, realized net gain (loss), and change in unrealized appreciation (depreciation) from an affiliated company of the portfolio were \$14,000, \$2,000, and \$1,000, respectively. Purchases and sales are for temporary cash investment purposes.

Statement of Changes in Net Assets

	Six Months Ended June 30, 2019	Year Ended December 31, 2018
	(\$000)	(\$000)
Increase (Decrease) in Net Assets		
Operations		
Net Investment Income	16,106	30,686
Realized Net Gain (Loss)	5,261	53,322
Change in Unrealized Appreciation (Depreciation)	163,924	(141,621)
Net Increase (Decrease) in Net Assets Resulting from Operations	185,291	(57,613)
Distributions		
Net Investment Income	(30,595)	(30,725)
Realized Capital Gain ¹	(55,292)	(37,675)
Total Distributions	(85,887)	(68,400)
Capital Share Transactions		
Issued	74,912	145,927
Issued in Lieu of Cash Distributions	85,887	68,400
Redeemed	(77,492)	(200,093)
Net Increase (Decrease) from Capital Share Transactions	83,307	14,234
Total Increase (Decrease)	182,711	(111,779)
Net Assets		
Beginning of Period	965,069	1,076,848
End of Period	1,147,780	965,069

¹ Includes fiscal 2019 and 2018 short-term gain distributions totaling \$6,455,000 and \$441,000, respectively. Short-term gain distributions are treated as ordinary income dividends for tax purposes.

Financial Highlights

For a Share Outstanding Throughout Each Period	Six Months Ended June 30,	Year Ended December 31,				
	2019	2018	2017	2016	2015	2014
Net Asset Value, Beginning of Period	\$11.57	\$13.14	\$13.48	\$13.77	\$14.17	\$11.87
Investment Operations						
Net Investment Income	.185 ¹	.367 ¹	.375 ¹	.346	.358	.307
Net Realized and Unrealized Gain (Loss) on Investments	1.998	(1.084)	.220	.734	(.032)	3.061
Total from Investment Operations	2.183	(.717)	.595	1.080	.326	3.368
Distributions						
Dividends from Net Investment Income	(.368)	(.383)	(.336)	(.375)	(.251)	(.367)
Distributions from Realized Capital Gains	(.665)	(.470)	(.599)	(.995)	(.475)	(.701)
Total Distributions	(1.033)	(.853)	(.935)	(1.370)	(.726)	(1.068)
Net Asset Value, End of Period	\$12.72	\$11.57	\$13.14	\$13.48	\$13.77	\$14.17
Total Return	19.24%	-5.35%	4.78%	8.36%	2.22%	30.11%
Ratios/Supplemental Data						
Net Assets, End of Period (Millions)	\$1,148	\$965	\$1,077	\$1,093	\$990	\$1,009
Ratio of Total Expenses to Average Net Assets	0.26%	0.26%	0.27%	0.27%	0.27%	0.27%
Ratio of Net Investment Income to Average Net Assets	2.94%	3.04%	2.87%	2.55%	2.60%	3.96%
Portfolio Turnover Rate	9%	35%	10%	14%	21%	11%

The expense ratio, net investment income ratio, and turnover rate for the current period have been annualized.

¹ Calculated based on average shares outstanding.

Notes to Financial Statements

The Real Estate Index 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. Temporary cash investments are valued using the latest bid prices or using valuations based on a matrix system (which considers such factors as security prices, yields, maturities, and ratings), both as furnished by independent pricing services.

2. **Futures Contracts:** The portfolio uses index futures contracts to a limited extent, with the objectives of maintaining full exposure to the stock market, maintaining liquidity, and minimizing transaction costs. The portfolio may purchase futures contracts to immediately invest incoming cash in the market, or sell futures in response to cash outflows, thereby simulating a fully invested position in the underlying index while maintaining a cash balance for liquidity. The primary risks associated with the use of futures contracts are imperfect correlation between changes in market values of stocks held by the portfolio and the prices of futures contracts, and the possibility of an illiquid market. Counterparty risk involving futures is mitigated because a regulated clearinghouse is the counterparty instead of the clearing broker. To further mitigate counterparty risk, the portfolio trades futures contracts on an exchange, monitors the financial strength of its clearing brokers and clearinghouse, and has entered into clearing agreements with its clearing brokers. The clearinghouse imposes initial margin requirements to secure the portfolio's performance and requires daily settlement of variation margin representing changes in the market value of each contract. Any assets pledged as initial margin for open contracts are noted in the Statement of Net Assets.

Futures contracts are valued at their quoted daily settlement prices. The notional amounts of the contracts are not recorded in the Statement of Net Assets. Fluctuations in the value of the contracts are recorded in the Statement of Net Assets as an asset (liability) and in the Statement of Operations as unrealized appreciation (depreciation) until the contracts are closed, when they are recorded as realized futures gains (losses).

During the six months ended June 30, 2019, the portfolio's average investments in long and short futures contracts represented less than 1% and 0% of net assets, respectively, based on the average of the notional amounts at each quarter-end during the period.

3. **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 for the period ended June 30, 2019, and has concluded that no provision for federal income tax is required in the portfolio's financial statements.

4. **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.

5. **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.

6. **Credit Facility:** The portfolio and certain other funds managed by The Vanguard Group ("Vanguard") participate in a \$4.3 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 June 30, 2019, or at any time during the period then ended.

7. **Other:** Distributions received from investment securities are recorded on the ex-dividend date. Each investment security typically reports annually the tax character of its distributions. Dividend income, capital gain distributions received, and unrealized appreciation (depreciation) reflect the amounts of taxable income, capital gain, and return of capital reported by the investment securities, and management's estimates of such amounts for investment security distributions for which actual information has not been reported. Interest income includes income distributions received from Vanguard Market Liquidity Fund and is accrued daily. Premiums and discounts on debt securities are amortized and accreted, respectively, to interest income over the lives of the respective securities, except for premiums on certain callable debt securities that are amortized to the earliest call date. 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. In accordance with the terms of a Funds' Service Agreement (the "FSA") between Vanguard and the portfolio, Vanguard furnishes to the portfolio investment advisory, 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 June 30, 2019, the portfolio had contributed to Vanguard capital in the amount of \$56,000, representing 0.00% 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.

C. 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.

The following table summarizes the market value of the portfolio's investments as of June 30, 2019, based on the inputs used to value them:

Investments	Level 1 (\$000)	Level 2 (\$000)	Level 3 (\$000)
Common Stocks	1,145,196	—	35
Temporary Cash Investments	4,372	99	—
Futures Contracts—Assets ¹	10	—	—
Total	1,149,578	99	35

¹ Represents variation margin on the last day of the reporting period.

D. As of June 30, 2019, gross unrealized appreciation and depreciation for investments and derivatives based on cost for U.S. federal income tax purposes were as follows:

	Amount (\$000)
Tax Cost	1,110,436
Gross Unrealized Appreciation	171,791
Gross Unrealized Depreciation	(132,561)
Net Unrealized Appreciation (Depreciation)	39,230

E. During the six months ended June 30, 2019, the portfolio purchased \$63,621,000 of investment securities and sold \$47,710,000 of investment securities, other than temporary cash investments.

F. Capital shares issued and redeemed were:

	Six Months Ended June 30, 2019	Year Ended December 31, 2018
	Shares (000)	Shares (000)
Issued	5,929	12,072
Issued in Lieu of Cash Distributions	7,040	6,005
Redeemed	(6,137)	(16,621)
Net Increase (Decrease) in Shares Outstanding	6,832	1,456

At June 30, 2019, one shareholder, an insurance company separate account whose holdings in the portfolio represent the indirect investment of Vanguard Variable Annuity contract holders, was the record or beneficial owner of 45% of the portfolio's net assets. If this shareholder were to redeem its investment in the portfolio, the redemption might result in an increase in the portfolio's expense ratio, cause the portfolio to incur higher transaction costs, or lead to the realization of taxable capital gains.

G. Management has determined that no events or transactions occurred subsequent to June 30, 2019, that would require recognition or disclosure in these financial statements.

Trustees Approve Advisory Arrangement

The board of trustees of Vanguard Variable Insurance Fund Real Estate Index Portfolio has renewed the portfolio's investment advisory arrangement with The Vanguard Group, Inc. (Vanguard), through its Equity Index Group. The board determined that continuing the portfolio's internalized management structure was in the best interests of the portfolio and its shareholders.

The board based its decision upon an evaluation of the advisor's investment staff, portfolio management process, and performance. This evaluation included information provided to the board by Vanguard's Portfolio Review Department, which is responsible for fund and advisor oversight and product management. The Portfolio Review Department met regularly with the advisor and made monthly presentations to the board during the fiscal year that directed the board's focus to relevant information and topics.

The board, or an investment committee made up of board members, also received information throughout the year during advisor presentations. For each advisor presentation, the board was provided with letters and reports that included information about, among other things, the advisory firm and the advisor's assessment of the investment environment, portfolio performance, and portfolio characteristics.

In addition, the board received monthly reports, which included a Market and Economic Report, a Fund Dashboard Monthly Summary, and a Fund Performance Report.

Prior to their meeting, the trustees were provided with a memo and materials that summarized the information they received over the course of the year. They also considered the factors discussed below, among others. However, no single factor determined whether the board approved the arrangement. Rather, it was the totality of the circumstances that drove the board's decision.

Nature, extent, and quality of services

The board reviewed the quality of the portfolio's investment management services over both the short and long term and took into account the organizational depth and stability of the advisor. The board considered that Vanguard has been managing investments for more than four decades. The Equity Index Group adheres to a sound, disciplined investment management process; the team has considerable experience, stability, and depth.

The board concluded that Vanguard's experience, stability, depth, and performance, among other factors, warranted continuation of the advisory arrangement.

Investment performance

The board considered the short- and long-term performance of the portfolio, including any periods of outperformance or underperformance compared with its target index and peer group. The board concluded that the performance was such that the advisory arrangement should continue.

Cost

The board concluded that the portfolio's expense ratio was well below the average expense ratio charged by funds in its peer group and that the portfolio's advisory expenses were also well below the peer-group average.

The board does not conduct a profitability analysis of Vanguard because of Vanguard's unique structure. Unlike most other mutual fund management companies, Vanguard is owned by the funds it oversees.

The benefit of economies of scale

The board concluded that the portfolio's arrangement with Vanguard ensures that the portfolio will realize economies of scale as it grows, with the cost to shareholders declining as portfolio assets increase.

The board will consider whether to renew the advisory arrangement again after a one-year period.

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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.

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.