

**Lincoln Variable Insurance Products Trust**  
**President's Letter**

Dear Fellow Investors,

After a challenging 2022 that saw elevated volatility and dismal returns for most asset classes, 2023 has been a year of remarkable resilience for the U.S. economy and global financial markets. Despite many headwinds, including restrictive monetary policy, a regional bank crisis, and geopolitical turmoil, the U.S. economy continued its surprisingly strong growth trajectory. The U.S. quarterly GDP growth rate accelerated to 4.9% in the third quarter of 2023. The U.S. unemployment rate stayed near the lowest level in the past five decades, indicating a tight labor market. In general, consumer spending and corporate balance sheets remained robust.



The U.S. Federal Reserve ("Fed") increased the Fed Funds Target Rate further by 100 bps throughout 2023 to a peak rate of 5.5%, reaching the highest level since the beginning of the 21<sup>st</sup> century. In late October, the U.S. 10-year Treasury Yield reached the highest level since mid-2007 before the Great Financial Crisis. As inflation cools, the Fed appears to be at the end of its rate hiking cycle. Fixed income returns became positive in 2023 despite the unprecedented bond bear market. The Bloomberg U.S. Aggregate Bond Index and the Bloomberg U.S. Treasury Index posted modestly positive returns, ending their two-year losing streaks. Moreover, the Bloomberg U.S. Corporate High Yield Bond Index returned 13.4%, as credit spreads were tight and the default rate was relatively low despite recent uptrends.

Fueled by economic resilience and optimism, domestic equity markets delivered stellar returns. The S&P 500 Index returned 26.3% during 2023, while the Nasdaq Composite Index returned 44.6% over that same period. As measured by the CBOE Volatility Index (VIX), stock market volatility dropped to the lowest level for the first time since the COVID-19 pandemic. There were wide dispersions across investment styles and geographies. With a sharp reversal from 2022, and a rotation of market leadership, U.S. large cap outperformed small cap, and growth equity outperformed value equity. Stock market leadership, however, was very narrow and highly concentrated on several mega-cap stocks in addition to other beneficiaries of explosive Generative AI growth. The largest seven companies within the S&P 500 Index, referred to as "the Magnificent Seven," were up more than 76% in 2023, dominating the impressive index performance. Non-U.S. equities in developed markets also had double-digit positive returns of 18.2% as measured by the MSCI EAFE Net Total Return USD Index, but lagged domestic equities, while emerging market equities continued to underperform by a large margin.

As we move into 2024, we believe that three key macroeconomic themes are front and center:

**Continuation of disinflation and likely interest rate cuts by the Fed** – While the path of disinflation could be bumpy, most of the key components of the Consumer Price Index have either come down or grown more slowly. Energy and commodity prices have dropped throughout the year. West Texas Intermediate (WTI) crude oil spot price declined from \$80.3 a barrel at the end of 2022 to \$71.7 at the end of 2023, which drove down national gasoline prices. Shelter inflation has been stubbornly high but should start to abate, given rising vacancy rates, ample housing supply, and reduced rental costs. In addition, global supply chains have normalized, and the labor market has cooled despite the low unemployment rate. It is widely expected that disinflation will continue into 2024, therefore, inflation readings will soften further and likely approach the Fed's long-term target. The substantial progress in controlling inflation will enable the Fed to shift monetary policy from tightening to neutral or easing. As stated in their most recent dot plot, the Fed projected three 25 bp rate cuts in 2024, and more in the following two years. Historically, such monetary policy pivots without an imminent economic recession have been beneficial tailwinds to capital market returns for both equities and bonds.

**Political uncertainty and policy implications from U.S. elections** – Since the end of World War II, the S&P 500 Index has never posted negative total returns in election years when the incumbent U.S. president was seeking re-election. The average returns in such election years were above the long-term average of all calendar years. However, as one of the more unique presidential elections in recent history, this presidential race may bring uncertainty and possible disruptions to the capital markets. Furthermore, there could be diverging and profound implications from the elections on fiscal, health care, industrial, trade, energy, and other policies. These policy implications may benefit or disadvantage different market participants within various sectors and industries.

**Crosscurrents of cyclical dynamics and secular trends** – There are many other cyclical dynamics and possible risks on the horizon. Personal consumption, the largest component of U.S. GDP, remained resilient. But consumer spending has been softening, as the excess savings from the pandemic era have been drawn down and nearing depletion. After the strong nonfarm payroll growth every month since the beginning of 2021, total U.S. job openings have decreased considerably in 2023, and the unemployment rate may tick up from current low levels. Monetary policy, including the ending of Fed tightening, tends to have long and variable lagging effects on the U.S. economy. The lagged effects are finally taking hold, and the U.S. economy is expected to grow at a slower rate in 2024, according to the Fed. These dynamics, and the Fed's shifting policy stance, are driving interest rates down and spurring equity and bond market rallies. On the other hand, there are certain counteracting secular trends. With great power competitions and geopolitical tensions, coupled with the ongoing deglobalization, fragmentations across supply chains, economies, and markets worldwide will increase. Regardless of the election outcomes, it is likely that the large federal government budget deficit will continue, if not be exacerbated, adding to burgeoning national debt and interest payment burdens in the years and decades to come. These secular trends may give rise to inflationary pressures and have long-term impacts and repercussions that are yet to fully manifest. In the foreseeable future, very few expect to see a near-zero ultra-low interest rate environment again, like the one witnessed in the previous decade.

As a post-rate hike new market cycle commences, the above macroeconomic themes and trends could lead to broader return dispersions, better potential for alpha generation from active investing, and more opportunities for less efficient asset classes and markets, especially private markets that may go mainstream in the next decade. As such, it is important to evaluate the risks in your portfolio with your financial advisor to ensure you stay invested and properly diversified based on your time horizon, financial goals, and risk tolerance. We are continuing to enhance our LVIP funds to provide a more robust and cost-effective universe of actively managed, rules-based, and passive investment options across major asset classes, including equity, fixed income, and multi-asset, that can help you achieve your unique objectives.

We hope you find the materials included in this annual report helpful as you evaluate your investments with us. Thank you for your continued trust in Lincoln Financial Group, and we wish you a healthy and prosperous 2024.

Sincerely,



Jayson R. Bronchetti, CFA, CAIA  
President, Lincoln Variable Insurance Products Trust