

Virtus Multi-Sector Fixed Income Fund

Market Overview

The overall economic picture remains supportive of fixed income spread sectors as the economic growth outlook is still positive yet subdued enough to likely keep inflation at low levels and the Federal Reserve from raising short term interest rates in the immediate future.

During the quarter ended December 31, 2011, fixed income spread sectors were helped by an improving U.S. macroeconomic environment, positive credit fundamentals, and continued demand for spread product. However, the European debt crisis and overall global growth uncertainty caused volatility during the quarter. Despite these headwinds, most spread sectors outperformed U.S. Treasuries. Yields were unchanged on the short end of the curve during the quarter, while the long end decreased slightly, causing a slight flattening of the curve.

Performance Review

The Virtus Multi-Sector Fixed Income Fund (Class A shares at NAV) outperformed its benchmark, the Barclays Capital U.S. Aggregate Bond Index, for the quarter.

The outperformance of fixed income spread sectors relative to U.S. Treasuries was the key driver of the Fund's strong performance for the quarter. In terms of sectors, the Fund's allocation to emerging markets high yield securities, corporate high yield securities, high yield bank loans, and non-agency commercial mortgage-backed securities were positive contributors to performance for the quarter. There were no significant performance detractors for the quarter as most spread sectors outperformed U.S. Treasuries, however, the Fund's overweight to financials in the corporate high-quality sector hurt performance during the quarter.

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Both the high yield bank loan and corporate high yield sectors benefited from a combination of factors, including strong fundamentals, positive earnings, and a decline in the projected default rate. Technical conditions continued to be positive for high yield during the quarter, resulting from positive fund flows into the sector.

The commercial mortgage-backed securities sector benefited from many factors, including a scarcity of bonds, an improving U.S. macroeconomic picture, improving fundamentals, and attractive relative value versus other sectors.

Over the quarter, changes in the Fund's sector exposure included a decrease in corporate high quality securities and high yield bank loans. Sale proceeds and Fund inflows were primarily invested in corporate high yield and residential mortgage-backed securities.

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SYMBOL (CUSIP)

A: NAMFX (92828R677)

C: NCMFX (92828R651)

I: VMFIX (92828R289)

INVESTMENT PROFESSIONAL

David L. Albrycht, CFA
Chief Investment Officer –
Multi-Sector Fixed Income Strategies
Industry start date: 1985
Start date with the fund: 1994

The Virtus Multi-Sector Fixed Income Fund seeks diversification across 14 sectors of the bond market through investments in intermediate duration bonds.

SECTOR ALLOCATIONS % Fund

Corporate - High Yield	32.24
Corporate - High Quality	17.26
Bank Loans	14.73
Non-Agency Commercial MBS	11.05
Non-USD	6.85
Emerging Market - High Yield	5.99
Yankee - High Quality	4.49
Non-Agency Residential MBS	2.05
Treasury	1.90
Asset-Backed Securities	1.84
Municipals	0.64
Cash	0.49
Taxable Municipals	0.32
Equity	0.09
Mortgage-Backed Securities	0.06

Sector weights are subject to change.

continued

Virtus Multi-Sector Fixed Income Fund

Outlook

We continue to be constructive on spread sectors due to attractive valuations and the modest economic growth that is expected to be supportive of these sectors. In particular, credit fundamentals remain strong in the corporate investment grade, corporate high yield, and bank loan sectors.

Given the recent volatility and the subsequent widening of yield spreads, most spread sectors are trading wider to their long-term averages, and when combined with strong fundamentals, they offer attractive valuations and compelling investment opportunities. Although we remain positive on spread sectors and have seen recent improvement in the U.S. economy, market headwinds still exist. A resolution to the European debt crisis remains uncertain, unemployment remains elevated, the housing market struggles to recover, and the overall strength of the global economy remains in question. Despite these challenges, conditions in the fixed income market remain substantially improved compared to the credit crunch of 2008 and early 2009.

We will maintain diversification in all of our credit-intensive sectors. We will look to be tactical with corporate credit, adding selectively on weakness, and we will consider corporate alternatives such as commercial mortgage-backed securities and taxable municipals when it would be favorable for the Fund. Within the commercial mortgage-backed securities sector, we prefer higher quality securities with high levels of credit enhancement and low leverage.

We are cautiously positive on the outlook for non-U.S. dollar bonds, favoring those that are denominated in currencies that typically benefit from a rise in commodity prices, have positive fundamentals, and have a yield advantage versus U.S. Treasury bonds. At the same time, however, volatility is likely to remain high within the sector due to environmental factors such as continued European sovereign fiscal concerns and global economic growth uncertainties.

Based on the current environment, we see the potential for outperformance as we get more clarity on the sustainability and strength of the economic recovery, evidence that the Chinese government has successfully engineered a soft landing for its economy, increased certainty that the U.S. is not entering recession, and clarity around Europe's fiscal concerns. We believe the Fund is well positioned to capitalize on opportunities as they arise, and we will take advantage of any weakness in either sectors or individual issues that may create value. This strategy has proven successful over the years, as demonstrated by our investment performance.

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Annualized Performance Class A as of 12/30/11 in percent

	QTD	YTD	1 Year	3 Year	5 Year	10 Year	Since Inception 12/15/1989	
NAV	3.79	3.19	3.19	18.49	5.80	7.11	7.71	<i>QTD, YTD and 1 Year performance is not annualized. Benchmark since inception performance is reported from 12/29/1989. Class A operating expenses are 1.16%.</i>
POP	-0.10	-0.68	-0.68	16.99	4.99	6.70	7.52	
Index	1.12	7.84	7.84	6.77	6.50	5.78	7.02	

Average annual total returns reflect the change in share price and the reinvestment of all dividends and capital gains. Net Asset Value (NAV) returns do not reflect the deduction of any sales charges. POP (Public Offering Price) performance reflects the deduction of the maximum sales charge of 3.75%. A contingent deferred sales charge of 0.50% may apply on certain redemptions made within 18 months following purchases on which a finder's fee has been paid.

Performance data quoted represents past results. Past performance is no guarantee of future results and current performance may be higher or lower than the performance shown. Investment return and principal value will fluctuate so your shares, when redeemed, may be worth more or less than their original cost. Please visit Virtus.com for performance data current to the most recent month-end.

Notes on Risk: As interest rates rise, existing bond prices fall and can cause the value of an investment to decline. Changes in interest rates will affect the value of longer-term fixed income securities more than shorter-term securities. Investing in **high yield bonds** may subject the portfolio to greater credit and market risks. Investing **internationally**, especially in **emerging markets**, involves additional risks such as currency, political, accounting, economic and market risk. The principal on **mortgage- or asset-backed securities** may normally be prepaid at any time, which will reduce the yield and market value of these securities.

Index: The Barclays Capital U.S. Aggregate Bond Index measures the U.S. investment grade fixed rate bond market. The index is calculated on a total return basis. The index is unmanaged and not available for direct investment.

The commentary is the opinion of the subadviser. This material has been prepared using sources of information generally believed to be reliable; however, its accuracy is not guaranteed. Opinions represented are subject to change and should not be considered investment advice or an offer of securities.

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