

Virtus Multi-Sector Short Term Bond 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 Short Term Bond Fund (Class A shares at NAV) outperformed its benchmark, the BofA Merrill Lynch 1-2.99 Year Medium Quality Corporate Bonds 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.

The emerging markets high yield sector benefited from many factors during the quarter, including positive fundamentals in the form of strong balance sheets, better fiscal management, and favorable growth estimates, along with the search for greater yield by investors.

Both the high yield bank loans 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 agency mortgage backed-securities and asset-backed securities. Sale proceeds and fund inflows were primarily invested in corporate high yield, emerging markets high yield securities, and Yankee high-quality securities.

“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. ... There were no significant performance detractors for the quarter as most spread sectors outperformed U.S. Treasuries...”

SYMBOL (CUSIP)

A: NARAX (92828R644)

C: PSTCX (92828R628)

I: PIMSX (92828R610)

T: PMSTX (92828R594)

INVESTMENT PROFESSIONAL

David L. Albrycht, CFA

Chief Investment Officer –

Multi-Sector Fixed Income Strategies

Industry start date: 1985

Start date with the fund: 1993

The Virtus Multi-Sector Short Term Bond Fund seeks diversification with an emphasis on maintaining low volatility and overall short duration by investing in higher-quality, more liquid securities across 14 bond market sectors.

SECTOR ALLOCATIONS % Fund

Corporate - High Quality	19.06
Non-Agency Commercial MBS	16.00
Corporate - High Yield	12.90
Non-USD	10.98
Asset-Backed Securities	10.74
Bank Loans	10.69
Non-Agency Residential MBS	7.89
Yankee - High Quality	4.90
Emerging Market - High Yield	3.34
Mortgage-Backed Securities	2.47
Treasury	0.41
Municipals	0.34
Taxable Municipals	0.23
Equity	0.04

Sector weights are subject to change.

continued

Virtus Multi-Sector Short Term Bond 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 wide 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, and we will emphasize higher quality issues within most 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 to the Fund. Within the commercial mortgage-backed securities sector, we prefer higher quality securities with high levels of credit enhancement and low leverage.

“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.”

We are cautiously positive on the outlook for non-U.S. dollar bonds, favoring those that are denominated in currencies that typically benefit from an increase 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 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 portfolio 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.

Virtus Multi-Sector Short Term Bond Fund

Morningstar Ratings™ Class A as of 12/30/11

		Overall	3 Year	5 Year	10 Year
Virtus Multi-Sector Short Term Bond Fund	Load Waived	★★★★★	★★★★★	★★★★★	★★★★★
NARAX	With Load	★★★★★	★★★★★	★★★★	★★★★★
	Short-Term Bond	353 funds	353 funds	322 funds	179 funds

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

	QTD	YTD	1 Year	3 Year	5 Year	10 Year	Since Inception 7/6/1992
NAV	2.51	3.10	3.10	13.84	5.54	5.57	6.07
POP	0.20	0.78	0.78	12.98	5.06	5.33	5.95
Index	0.69	1.87	1.87	7.71	4.61	4.37	5.52

QTD, YTD and 1 Year performance is not annualized. Benchmark since inception performance is reported from 6/30/1992. Class A operating expenses are 1.07%.

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 2.25%. 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 BofA Merrill Lynch 1-2.99 Year Medium Quality Corporate Bonds Index measures performance of U.S. corporate bond issues rated BBB and A by Standard and Poor's with maturities between one and three years. The index is calculated on a total return basis. The index is unmanaged and not available for direct investment.

For each fund with at least a three-year history, Morningstar calculates a Morningstar Rating™ based on a Morningstar Risk-Adjusted Return measure that accounts for a variation in a fund's monthly performance (including the effects of sales charges, loads, and redemption fees), placing more emphasis on downward variations and rewarding consistent performance. The top 10% of funds in an investment category receive 5 stars, the next 22.5% receive 4 stars, the next 35% receive 3 stars, the next 22.5% receive 2 stars, and the bottom 10% receive 1 star. The Overall Morningstar Rating for a fund is derived from a weighted average of the performance figures associated with its 3-, 5-, and 10-year (if applicable) Morningstar Rating metrics. Ratings are for the A Shares as shown only; other share classes bear different fees and expenses, which affect performance.

Load-waived A share star ratings do not include any front-end sales load and are intended for those investors who have access to such purchase terms (e.g., plan participants of a defined contribution plan). Not all A share mutual funds for which Morningstar calculates a load-waived A share star rating may actually waive their front-end sales load. Therefore, Morningstar strongly encourages investors to contact their investment professional to determine whether they are eligible to purchase the A share without paying the front load.

© 2012 Morningstar, Inc. All rights reserved. The information contained herein: (1) is proprietary to Morningstar and/or its content providers; (2) may not be copied or distributed; and (3) is not warranted to be accurate, complete, or timely. Neither Morningstar nor its content providers are responsible for any damages or losses arising from any use of this information. Past performance is no guarantee of future results.

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.

Please carefully consider the Fund's investment objectives, risks, charges and expenses before investing. For this and other information about any Virtus mutual fund, call 1-800-243-4361 or visit Virtus.com for a prospectus. Read it carefully before you invest or send money.

Not insured by FDIC/NCUSIF or any federal government agency. No bank guarantee. Not a deposit. May lose value.

Distributed by VP Distributors, LLC, member FINRA and subsidiary of Virtus Investment Partners, Inc.

2001 1-12 © 2012 Virtus Investment Partners, Inc.