

Virtus Seix High Yield Fund

A: HYPX (92837F698) | I: SAMX (92837F672) | R: HYSX (92837F680) | R6: HYIZ (92837F664)

MARKET REVIEW

The high yield sector posted a negative return (-1.11%) in the first quarter as measured by the ICE BofAML BB/B Constrained Index. Given only moderate spread widening, the move in U.S. Treasury rates during the quarter was the main driver of returns. On a credit quality basis, the higher-rated, more interest-rate sensitive segments of the market underperformed with BBs posting a return of -1.66% followed by Bs at -0.40%.

In terms of new issue activity, first quarter volume on a gross basis was about 25% lower than the year-ago period with a significant percentage being used for refinancing activity. The percentage of refinancing this year (74%) is higher than 2017 (64%), which means that the net amount to the high yield market is fairly low. In terms of demand, flows have been negative for the asset class.

Fundamentals for the high yield issuer universe continue to be favorable and are expected to remain so at least in the near term. Default activity, however, did pick up during the quarter, but was fairly concentrated and notably included Claire's stores and iHeart Communications.

For more on our high yield market commentary, read our [first quarter Leveraged Finance Market Review and Outlook](#).

PERFORMANCE

The Virtus Seix High Yield Fund's quarterly return of -0.87% was 24 basis points ahead of the -1.11% return of the benchmark. The positive effects of favorable security selection in finance, technology, energy, and cable were partially offset by the negative effects of unfavorable security selection in telecommunications.

CURRENT STRATEGY

Though fundamentals are overall positive and technicals neutral, the potential for spread tightening is limited. As a strategic decision, we are focusing on upgrading the quality of portfolios. We are also mindful of the increased sensitivity to changes in interest rates as investors go up the quality spectrum in high yield. Therefore, in this Fund, which is typically either void or substantially underweighted in CCCs, we are balancing the interest rate risk in BBs against the additional credit risk in Bs and are currently overweighting Bs. Despite relatively narrow spreads, market volatility is presenting potential opportunities to pick up incremental yield such as we did in March in the cable and energy sectors. Aside from these one-off situations, however, our focus is on quality over yield.

OUTLOOK

With fundamentals for most issuers continuing to be stable, we expect that defaults will remain below the historic average this year and in line with 2017. While high yield mutual fund flows have been negative, supply has been able to adjust while a segment of issuers tap the leveraged loan market where demand from collateralized loan obligations stays robust. With the return of volatility in 2018, high yield behaved in line with expectations. As interest rates rose in the first quarter, high yield outperformed investment grade benchmarks (-0.86% vs. -1.46 for the Bloomberg Barclays Aggressive Bond Index) owing to the sector's lower duration and higher income. High yield also offered returns not too different from equities (-0.76% for the S&P 500® Index) but at a much lower level of volatility (annualized standard deviation of 19.17 for the S&P 500 in March vs. 1.96 for high yield). We expect that uncertainty about interest rates and economic growth may continue to impact the path of high yield returns, but that the relatively stable fundamentals will anchor performance over the next twelve months.

Virtus Seix High Yield Fund

INVESTMENT ADVISER

Virtus Fund Advisers, LLC

INVESTMENT SUBADVISER

Seix Investment Advisors LLC

PORTFOLIO MANAGERS



Michael Kirkpatrick
Industry start date: 1991
Start date with Fund: 2007



James FitzPatrick, CFA
Industry start date: 1996
Start date with Fund: 2013

SECTOR ALLOCATIONS

% Fund

Other Industries	44.45
Energy	17.26
Bank/Finance/Insurance	11.00
Telecom	9.10
Healthcare	9.06
Cable & Satellite TV	7.40
Cash & Equivalents	1.73

Sector weights are subject to change.

AVERAGE ANNUAL TOTAL RETURNS (%) as of 3/31/18

	QTD	YTD	1 Year	3 Year	5 Year	10 Year	Since Inception 12/29/2000
Fund Class I	-0.87	-0.87	3.73	3.71	3.86	6.49	6.68
Index	-1.11	-1.11	3.43	4.74	4.85	7.44	7.29

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.

The fund class gross expense ratio is 0.81%. The net expense ratio is 0.65%, which reflects a contractual expense reimbursement in effect through 7/31/2019. This ratio reflects the direct and indirect expenses paid by the Fund.

The net expense ratio minus the indirect expenses incurred by the underlying funds in which the Fund invests is 0.64%.

Average annual total return is the annual compound return for the indicated period and reflects the change in share price and the reinvestment of all dividends and capital gains. Returns for periods of one year or less are cumulative returns. Class I shares have no sales charges or distribution or service fees, therefore their returns do not reflect these expenses. Fees and expenses vary, and other share classes are subject to sales charges and fees. Class I shares are offered primarily to eligible institutional investors who purchase the minimum amounts required as described in the prospectus and may not be available to all investors. For fund performance on other share classes, please visit www.virtus.com.

Index: The **ICE BofAML US High Yield BB-B Constrained Index** measures performance of BB/B U.S. dollar denominated corporate bonds publicly issued in the U.S. domestic market, and is restricted to a maximum of 2% per issuer. The index is calculated on a total return basis. The index is unmanaged, its returns do not reflect any fees, expenses, or sales charges, and is not available for direct investment.

Notes on Risk: Notes on Risk: Credit & Interest: Debt securities are subject to various risks, the most prominent of which are credit and interest rate risk. The issuer of a debt security may fail to make interest and/or principal payments. Values of debt securities may rise or fall in response to changes in interest rates, and this risk may be enhanced with longer-term maturities. **High Yield-High Risk Fixed Income Securities:** There is a greater level of credit risk and price volatility involved with high yield securities than investment grade securities. **Prospectus:** For additional information on risks, please see the fund's prospectus.

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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