

Virtus KAR Mid-Cap Core Fund

A: VMACX (92828N114) | C: VMCCX (92828N122) | I: VIMCX (92828N130) | R6: VRMCX (92828N262)

MARKET REVIEW

Domestic equities recovered during the second quarter, erasing the losses incurred in the first few months of the year. The S&P 500® Index gained 3.43%, and small stocks performed even better with the Russell 2000® Index returning 7.75%. Within international equities, a continued escalation in trade-war rhetoric negatively impacted developed and emerging market stocks. The MSCI EAFE® Index declined 1.24% in the quarter, and the MSCI Emerging Markets Index fell 7.96%. The 10-year U.S. Treasury yield moved up, hitting 2.86%, but the yield curve continued to flatten as the difference between the 10-year and 2-year rates collapsed to a multi-year low.

PERFORMANCE

The Fund (Class I) returned 3.02% for the quarter, outperforming the 2.82% return of the Russell Midcap® Index. Performance was driven by strong stock selection in the technology and consumer staples sectors. Gains were partially offset by an underweight in the energy sector and negative stock selection in the materials and processing sector.

Tractor Supply Co. and Aspen Technology were the biggest contributors to performance in the quarter.

- > Retailer Tractor Supply reported solid same-store sales and marked the first quarter of neutral deflation in 17 consecutive quarters. The company plans to reinvest proceeds from a lower tax rate into higher store payroll, as well as into IT and a new point-of-sale system.
- > Software company Aspen Tech reported strong demand for its newest product suite, Asset Performance Management. Revenue growth accelerated, due in part to the company's investments to support this new offering. While this has muted some of Aspen's profitability growth in the short term, it should support sustainable growth over a longer time horizon. In the interim, the company continues to be very active in share repurchases.

WABCO Holdings and Signature Bank detracted the most from performance in the quarter.

- > Vehicle control systems manufacturer WABCO's recent financial results showed organic growth in revenues and an improvement in profit margins. Management increased its guidance for the year following the strong results, but the company's shares have remained weak due to fears of rising inflation and the potential drag that tariffs could create on heavy-duty truck demand.

We have no special insight regarding inflation and tariffs, so we remain focused on assessing the strength of the company's competitive position, which remains intact. Many tailwinds remain for WABCO to continue to outgrow global commercial-truck production by increasing its content per vehicle. As a result, we remain owners of the business.

- > Signature Bank shares have underperformed for a while due to the flattening of the yield curve, which puts pressure on the margins the bank makes on its loans, as well as multiple write-downs in its taxi medallion portfolio due to competition from ride-sharing companies. The trend continued in the recent quarter. Despite the near-term headwinds, Signature remains one of the most efficient banks in the U.S., with loan growth and long-term profitability metrics well above those of its peers. We believe these headwinds are not structural and the bank's true earnings power will soon re-emerge.

PORTFOLIO CHANGES

In the second quarter, we closed out of Manhattan Associates and made no new purchases for the portfolio.

- > Despite Manhattan Associates' status as a leading provider of vertical software, its attractive business model, and potential to be an essential element of a customer's supply-chain ecosystem, we have observed continued deterioration in the retail operating environment over the past several months. Aggressive price competition among software vendors has intensified as retail customers have increasingly chosen lower price over superior technology, which has negatively affected Manhattan's near- and medium-term outlook. With these considerations in mind, and the valuation of the shares being fair, we exited our small position.

OUTLOOK

Uncertainty continues to cast a shadow in the markets amid growing tension around global trade tariffs and what seems to be stalled growth in international markets. Still, U.S. business and economic activity appears to be solid, with various industries continuing in expansion mode and second quarter GDP growth estimated to be strong. As always, we remain focused on investing in high-quality companies that offer a sustainable competitive edge. In our view, this is the best long-term protection we can provide in this period of heightened uncertainty.

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INVESTMENT ADVISER

Virtus Investment Advisers, Inc.

INVESTMENT SUBADVISER

Kayne Anderson Rudnick Investment Management, LLC

PORTFOLIO MANAGERS



Jon Christensen, CFA
Industry start date: 1995
Start date with Fund: 2009



Craig Stone
Industry start date: 1989
Start date with Fund: 2009

TOP TEN HOLDINGS

% Fund

Globus Medical, Inc. Class A	5.37
Zoetis, Inc. Class A	5.06
Monster Beverage Corp.	4.88
Tractor Supply Co.	4.86
AMETEK, Inc.	4.85
Aspen Technology, Inc.	4.45
Broadridge Financial Solutions, Inc.	4.33
Cooper Companies, Inc.	4.01
Amphenol Corporation Class A	4.00
AMN Healthcare Services, Inc.	3.66

Holdings are subject to change.

AVERAGE ANNUAL TOTAL RETURNS (%) as of 6/30/18

	QTD	YTD	1 Year	3 Year	5 Year	10 Year	Since Inception 06/22/2009
Fund Class I	3.02	5.10	19.70	12.53	14.79	n/a	15.66
Index	2.82	2.35	12.33	9.58	12.22	n/a	16.48

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 1.23%. The net expense ratio is 0.96%, which reflects a contractual expense reimbursement in effect through 1/31/2019. 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 0.95%.

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 **Russell Midcap® Index** is a market capitalization-weighted index of medium capitalization stocks of U.S. companies. The index is calculated on a total return basis with dividends reinvested. 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: Equity Securities: The market price of equity securities may be adversely affected by financial market, industry, or issuer-specific events. Focus on a particular style or on small or medium-sized companies may enhance that risk. **Limited Number of Investments:** Because the fund has a limited number of securities, it may be more susceptible to factors adversely affecting its securities than a less concentrated fund. **Industry/Sector Concentration:** A fund that focuses its investments in a particular industry or sector will be more sensitive to conditions that affect that industry or sector than a non-concentrated fund.

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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