

Virtus KAR Small-Mid Cap Growth Fund

A: VAKSX (92836N817) | C: VCKSX (92836N791) | I: VIKSX (92836N783) | R6: VRKSX (92836N775)

MARKET REVIEW

Stocks produced mixed returns in the third quarter. Large-cap stocks, as measured by the S&P 500® Index, eked out a small gain of 0.58%. In contrast, small-cap stocks, as measured by the Russell 2000® Index, returned -4.36%. Large-cap growth stocks, as measured by the Russell 1000® Growth Index, generated a modestly positive return of 1.16%, and large-cap value stocks, as measured by the Russell 1000® Value Index, generated a modestly negative return of -0.78%. Year to date, value was up 16.14%, outperforming both the S&P 500 (15.92%) and Russell 1000 Growth (14.30%).

PORTFOLIO OVERVIEW

The Virtus KAR Small-Mid Cap Growth Fund returned -0.19% (Class I) in the quarter, outperforming the Russell 2500™ Growth Index, which returned -3.53%. Much of the outperformance was driven by stock selection with sector allocation also providing a modest benefit. Stock selection and an underweight position in the healthcare sector and stock selection in the industrials sector contributed positively to performance. Stock selection and an overweight position in the communication services sector and stock selection in the consumer staples sector detracted from performance.

The portfolio's overweight to high-quality names (as measured by S&P Quality Rankings with a ranking of B+ and above) contributed positively to performance. Also, the highest P/E stocks (those with a higher ratio of a company's share price to the company's earnings per share) outperformed during the quarter relative to stocks with lower P/Es, indicating more of a focus on growth names still early in their maturation. As we are overweight in higher P/E names, this also helped performance.

Ryan Specialty Group and Site One Landscape Supply were the largest contributors to performance in the quarter.

- > We participated in Ryan Specialty Group's IPO in the quarter. The international specialty insurance business subsequently reported a strong first quarter as a public company, causing the shares to appreciate.
 - > SiteOne Landscape Supply underperformed last quarter as investors worried about the forward growth of the business despite the company reporting a good quarter. This quarter, some of those worries dissipated as the company continued to see good organic daily sales and improving margins.
- MediaAlpha and Ollie's Bargain Outlet were the largest detractors from performance in the quarter.
- > Advertising technology company MediaAlpha has faced headwinds from auto insurers pulling back on new customer acquisition spending as lockdown measures have eased and miles driven have increased, leading to higher losses. The company also faced higher ad pricing from internet platforms, and investors were likely concerned that the demand and cost for leads could decline. In addition, the company announced its CFO was leaving. We view these issues as transitory and believe MediaAlpha is still well positioned to sustain long-term growth.

- > Throughout the COVID-19 pandemic, Ollie's Bargain Outlet remained open for business and benefited significantly in 2020 as the discount retailer generated robust revenue and comparable sales growth. Recently, Ollie's reported declines, in both revenue and comparable sales as outperforming 2020's numbers has proven difficult. Additionally, Ollie's replaced its senior vice president of supply chain as the company seeks to improve supply chain productivity. We view the short-term revenue and comparable sales declines as reasonable given the prior year's performance and believe the long-term competitive posture of the business remains intact.

PURCHASES AND SALES

During the quarter, we purchased Clearwater Analytics and Ryan Specialty Group Holdings (discussed above). We sold Lemonade and Oscar Health.

- > Clearwater Analytics provides investment accounting software, which is used by asset managers, corporate treasuries, and insurance companies for daily reconciliation of their holdings. The company specializes in reconciling more esoteric securities, where the need for accurate data is harder to obtain without scale.
- > Ryan Specialty Group Holdings engages in the provision of wholesale insurance brokerage, distribution, and underwriting services through its subsidiaries. Its specialties include wholesale brokerage, binding authority, and underwriting management. The company enjoys scale advantages against smaller competitors, which provide its insurance professionals more relationships with retail brokerages and therefore more policy submission opportunities.
- > We sold insurance companies Lemonade and Oscar Health (in tandem with our participation in the Ryan Specialty Group IPO) as we believe that the competitive landscape throughout disruptive insurance companies is still unsettled. Given the high costs of acquiring market share and the new approaches to qualifying risk, we believed it was better for insurance companies to be acting as brokers than underwriters and exited our small positions in both companies.

OUTLOOK

We believe interest rates and corporate profitability are the two most important variables affecting equity markets. The Federal Reserve's plan to taper its purchases of bonds starting in November has been well telegraphed to investors. Relatively benign rates and strong corporate profitability are a prescription for rising equity prices over time. However, we believe investors should expect a more selective market going forward with more muted equity returns in the range of 5% to 10%. It is more likely that the U.S. economy will continue to grow but at a more moderate and sustainable pace. We believe this should be an environment where stocks of high-quality businesses can perform well.

INVESTMENT ADVISER

Virtus Investment Advisers, Inc.

INVESTMENT SUBADVISER

Kayne Anderson Rudnick Investment Management, LLC

PORTFOLIO MANAGER



Julie Biel, CFA
 Industry start date: 2004
 Start date as Fund Portfolio Manager: 2020

TOP TEN HOLDINGS

% Fund

Old Dominion Freight Line Inc.	5.93
West Pharmaceutical Services Inc.	5.59
Bentley Systems Inc.	5.07
Silk Road Medical Inc.	4.84
SiteOne Landscape Supply Inc.	4.64
Copart Inc.	4.13
Avalara Inc.	3.99
Tyler Technologies Inc.	3.84
Ryan Specialty Group Holdings Inc.	3.83
HEICO Corp.	3.60

Holdings are subject to change.

TOP FIVE CONTRIBUTORS % Contribution

Ryan Specialty Group Holdings Inc.	1.16
SiteOne Landscape Supply Inc.	0.87
West Pharmaceutical Services Inc.	0.85
Clearwater Analytics Holdings Inc.	0.82
Old Dominion Freight Line Inc.	0.66

TOP FIVE DETRACTORS % Contribution

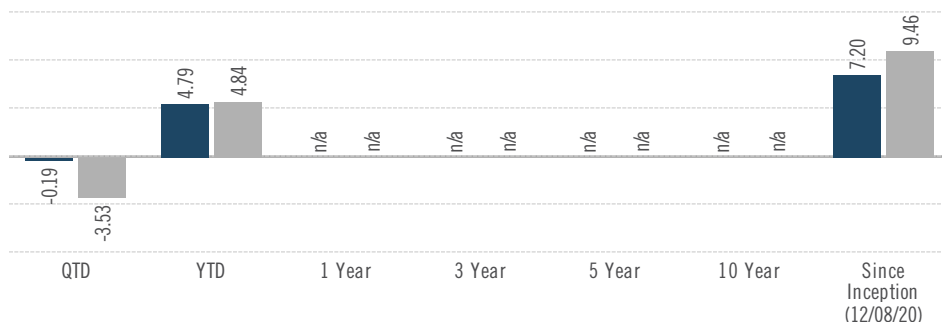
MediaAlpha Inc.	-1.67
Ollie's Bargain Outlet Holdings Inc.	-0.88
HealthEquity Inc.	-0.74
Lamb Weston Holdings Inc.	-0.61
Olo Inc.	-0.59

% Contribution: Absolute weighted contribution.

To obtain the top/bottom holdings calculation methodology, call 800-243-4361.

AVERAGE ANNUAL TOTAL RETURNS (%) as of 09/30/21

■ Fund Class Institutional ■ Index



Performance data quoted represents past performance. Past performance does not guarantee future results. Investment return and principal value will fluctuate so that shares, when redeemed, may be worth more or less than their original cost. Current performance may be lower or higher than the performance data quoted. Please visit virtus.com for performance data current to the most recent month end. This share class has no sales charges and is not available to all investors. Other share classes have sales charges. See virtus.com for details.

The fund class gross expense ratio is 1.14%. The net expense ratio is 1.05%, which reflects a contractual expense reimbursement in effect through 1/31/2022.

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.

Index: The **Russell 2500™ Growth Index** is a market capitalization-weighted index of growth-oriented stocks of the 2,500 smallest companies in the Russell Universe, which comprises the 3,000 largest 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 portfolio has a limited number of securities, it may be more susceptible to factors adversely affecting its securities than a portfolio with a greater number of securities. **Market Volatility:** Local, regional, or global events such as war, acts of terrorism, the spread of infectious illness or other public health issues, recessions, or other events could have a significant impact on the portfolio and its investments, including hampering the ability of the portfolio manager(s) to invest the portfolio's assets as intended. **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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