VIRTUS MUTUAL FUNDS

Virtus Newfleet Multi-Sector Intermediate Bond Fund

A: NAMFX (92828R677) | C: NCMFX (92828R651) | I: VMFIX (92828R289) | R6: VMFRX (92828W544)

MARKET OVERVIEW

The overall positive tone for fixed income spread sectors continued into the fourth quarter with short-lived bouts of increased volatility in October and November. Challenges to the status quo included continued geopolitical tensions and the turbulent political climate in Washington D.C. During the quarter, oil prices moved higher, U.S. economic data modestly improved, and tax reform legislation was passed. As expected, the Federal Reserve raised its target rate at the December FOMC meeting to a range of 1.25%-1.50%.

Most spread sectors outperformed U.S. Treasuries during the fourth quarter as spreads tightened and interest rates remained low.

For a more detailed review of the fourth quarter and our outlook, please see Newfleet's 4Q17 Market Review and 2018 Fixed Income Market Outlook.

HOW THE FUND PERFORMED

The Fund (Class I) outperformed its benchmark in the fourth quarter with a return of 0.76% versus the Bloomberg Barclays U.S. Aggregate Bond Index return of 0.39%. For the year, the Fund returned 7.34% versus 3.54% for the Index.

Contributors

> Our underweight to **U.S. Treasuries** benefited performance as most spread sectors outperformed the government sector.

> The **Corporate High Yield** sector was a primary contributor to performance during the quarter. The Fund's outperformance was driven by strong issue selection. Overall improving fundamentals and positive technicals (negative net supply) continued to be supportive of the sector.

> Allocation to the **Bank Loan** sector was a positive contributor as loans benefited from rising interest rates and positive supply and demand dynamics.

> The **Yankee High Quality** sector was a top contributor to performance. The Fund's outperformance within the sector was driven by country and issue selection. Overall fundamentals within the sector have shown signs of stabilizing as economic growth is recovering in the aggregate. The continued search for yield, strong risk sentiment, commodity price rebound, and accommodative central bank monetary policy has contributed towards positive performance in U.S. dollar-denominated foreign assets.

Detractors

> **Corporate High Quality:** The Fund's underweight to the sector versus the benchmark was detrimental to performance.

> **Non-U.S. Dollar Securities:** During the quarter, the U.S. dollar strengthened compared to the Fund's non-U.S. dollar bonds, which are concentrated in emerging market countries. This was due to prospects for U.S. tax reform and improving economic data, therefore negatively impacting our non-U.S. dollar holdings.

CURRENT FUND STRATEGY

Sector Changes: We reduced our exposure to U.S. Treasuries and emerging market high yield securities. We redeployed the sale proceeds primarily into corporate high yield and asset-backed securities (ABS).

Foreign Exposure: We slightly decreased the overall non-U.S. exposure within the Fund and continued to overweight emerging markets. Valuations in specific countries are attractive and fundamentals are slowly getting better with Brazil, Argentina, and Russia expected to drive improvements in 2018. The Fund's non-U.S. exposure could continue to receive an uplift from improving global growth, stronger than anticipated Chinese growth, a weaker U.S. dollar, supportive commodity prices, and accommodative monetary policy from major global central banks. European political events are passing without market disruptions. In this space, we favor sovereigns in larger capital structures. Total non-U.S. exposure remains below historical averages, but our total emerging market country exposure is above the five-year average for the Fund.

Securitized Product: Our allocation to non-agency residential mortgage-backed securities (RMBS) and ABS continues to play an important role. These segments of the market offer a diversified collateral base and attractive valuations relative to many other areas of the fixed income markets. They also offer diversification to the portfolio's corporate credit allocation. Our consumer focus within the ABS sector benefits from the U.S. consumer's continued ability to drive the U.S. economy. RMBS benefits from the continuing improvement in the housing market and demand for mortgage credit.

OUTLOOK

As we look ahead to 2018, we expect that spread sectors will continue to perform well in the current environment of steady GDP growth, subdued inflation, and a favorable macroeconomic backdrop. We are constructive on spread sectors based on sound and improving fundamentals, strong technicals, and still-accommodative central banks. We recognize, however, that valuations are fair to rich in many areas of the fixed income market. With spreads well inside of long-term averages, issue selection and positioning within sectors is critical. There are, of course, risks that include the unprecedented retreat from quantitative easing by the major central banks, oil price volatility, geopolitical tensions, economic developments in China, the path of the U.S. dollar, and continued gridlock in Washington, D.C.

As always, we believe it is important to stay diversified, have granular positions, and emphasize liquid investments. We will continue to look for opportunities in all sectors of the bond market, striving to uncover any out-of-favor or undervalued sectors and securities. With strong demand for fixed income by investors and a supportive environment, spread sectors continue to offer attractive investment opportunities to investors searching for total return and yield.

Effective May 8, 2017, the Fund's name was changed from Virtus Multi-Sector Intermediate Bond Fund.

Virtus Newfleet Multi-Sector Intermediate Bond Fund

INVESTMENT ADVISER

Virtus Investment Advisers, Inc.

INVESTMENT SUBADVISER

Newfleet Asset Management, LLC

INVESTMENT PROFESSIONALS

David L. Albrycht, CFA
Industry start date: 1985
Start date with the Fund: 1994

SECTOR ALLOCATIONS

	% Fund
Corporate - High Yield	28.79
Corporate - High Quality	21.98
Emerging Market - High Yield	9.57
Bank Loans	8.62
Non-Agency Residential MBS	8.50
Asset Backed Securities	6.05
Yankee - High Quality	5.33
Non-USD	3.75
Mortgage Backed Securities	2.86
Equity	2.45
Non-Agency Commercial MBS	1.07
Treasury	0.92
Taxable Municipals	0.11

Sector weights are subject to change.

AVERAGE ANNUAL TOTAL RETURNS as of 12/31/17 in percent

I Share	QTD	YTD	1 Year	3 Year	5 Year	10 Year	Since Inception 10/1/2009
NAV	0.76	7.34	7.34	5.29	4.02	n/a	6.67
Index	0.39	3.54	3.54	2.24	2.10	n/a	3.48

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 0.88%. The net expense ratio is 0.77%, 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 0.74%.

Average annual total returns reflect the change in share price and the reinvestment of all dividends and capital gains. Class I shares have no sales charge and therefore their returns do not reflect the deduction of a sales charge, which if applied, **would reduce the performance quoted**. Fees and expenses vary among share classes and other share classes do carry sales charges. Class I shares are offered primarily to eligible institutional investors who purchase the minimum amounts required and may not be available to all investors. For Fund Performance on other share classes, please visit www.virtus.com.

Index: The **Bloomberg Barclays 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, its returns do not reflect any fees, expenses, or sales charges, and it is not available for direct investment.

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. **Foreign & Emerging Markets:** Investing internationally, especially in emerging markets, involves additional risks such as currency, political, accounting, economic, and market risk. **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. **ABS/MBS:** Changes in interest rates can cause both extension and prepayment risks for asset- and mortgage-backed securities. These securities are also subject to risks associated with the repayment of underlying collateral. **Bank Loans:** Loans may be unsecured or not fully collateralized, may be subject to restrictions on resale and/or trade infrequently on the secondary market. Loans can carry significant credit and call risk, can be difficult to value and have longer settlement times than other investments, which can make loans relatively illiquid at times. **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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