

Virtus KAR Small-Cap Core Fund

A: PKSAX (92828N551) | C: PKSCX (92828N536) | I: PKSFX (92828N528) | R6: VSCRX (92828N429)

MARKET REVIEW

2023 proved to be an outstanding year for capital markets. At the start of the year, investors were braced for an imminent recession, but it never materialized, and the fourth quarter ended up being the strongest quarter of the year. Large-cap stocks, as measured by the S&P 500® Index, advanced 11.69% in the fourth quarter alone, bringing the year-to-date return to 26.29%. Large-cap growth stocks, as measured by the Russell 1000® Growth Index, gained 14.16% in the quarter, outperforming large-cap value stocks, as measured by the Russell 1000® Value Index, which returned 9.50%.

The “Magnificent Seven” mega-cap tech stocks (Alphabet, Amazon, Apple, Meta Platforms, Microsoft, NVIDIA, and Tesla) were responsible for most of the outperformance by large-cap growth stocks during the year. However, market breadth started to improve in the fourth quarter, as small-cap stocks, as measured by the Russell 2000® Index, advanced 14.03% in the quarter. Falling interest rates, due to the continued improvement in the inflation outlook, was the principal reason that equities performed so well during the quarter.

FUND PERFORMANCE

The Virtus KAR Small-Cap Core Fund returned 14.49% (Class I) in the quarter, outperforming the 14.03% return of the Russell 2000 Index. The Fund’s underweight in the energy sector, combined with stock selection in the industrials sector, contributed positively to performance, while stock selection in the financials and information technology sectors detracted from performance.

Simpson Manufacturing and CorVel contributed the most to performance during the quarter.

- > Simpson Manufacturing’s shares performed strongly following the building materials company’s reports of better-than-expected operating results and improved profitability.
- > Shares of risk management solutions provider CorVel outperformed after the company posted solid financial results driven by increased hiring in its sales team. CorVel’s fully integrated platform brings strong capabilities to customers, which are particularly vital in the current environment with the pandemic having dramatically expanded the use of telemedicine.

Atrion and RLI detracted the most from performance during the quarter.

- > Medical device manufacturer Atrion continues to be impacted by destocking at its largest customers. Some of these customers over-ordered during the pandemic and are now reducing their inventories. We do not believe the company is facing more intense competitive pressures, and we expect a return to growth in 2024.
- > Specialty insurer RLI’s shares declined modestly in the quarter as investors anticipated the potential for slowing interest rate increases across the property and casualty insurance industry as inflation moderates.

PORTFOLIO CHANGES

During the quarter, we purchased Kadant and UFP Industries for the portfolio, and we sold PriceSmart.

- > Kadant is a global supplier of highly engineered products and systems serving industrial process markets. Kadant supplies capital equipment and parts/consumables to customers across three business segments: industrial processing, flow control, and material handling.
- > UFP Industries is a manufacturer and supplier of wood, wood composite, and other products to retailers, the manufactured housing industry, residential and commercial construction, and other industrial customers.
- > We sold our position in warehouse retailer PriceSmart because the company struggled to operate its warehouse club retail model in Latin American countries in a way that generates persistently high returns on capital.

OUTLOOK

With the Federal Reserve’s hiking cycle likely behind us and corporate earnings growth likely to resume, we believe 2024 should be a favorable year for equity returns. Coming into 2024, investor sentiment is nowhere near as negative as it was coming into 2023, but there is still plenty of cash on the sidelines built up over the last year. As short-term interest rates decline and the yield curve moves to flat, or even positively sloped, we believe this capital will make its way into fixed income and equity markets. From our perspective, returns in 2024 are unlikely to be as robust as they were in 2023 but are likely to be in line with earnings growth. We also expect that 2024 will experience more volatility due to the U.S. presidential election, which is likely to be contentious.

Related Reading: [Q4 KAR Market Review & Outlook](#)

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 as Fund Portfolio Manager: 2008



Todd Bailey, CFA
Industry start date: 1999
Start date as Fund Portfolio Manager: 2009

TOP TEN HOLDINGS

	% Fund
Simpson Manufacturing Co. Inc.	8.28
EMCOR Group Inc.	7.11
FTI Consulting Inc.	6.21
Primerica Inc.	5.20
Manhattan Associates Inc.	5.05
Acushnet Holdings Corp.	4.77
CorVel Corp.	4.48
The Toro Co.	4.11
Watts Water Technologies Inc.	4.04
Landstar System Inc.	3.89

Holdings are subject to change.

TOP FIVE CONTRIBUTORS % Contribution

Simpson Manufacturing Co. Inc.	2.29
CorVel Corp.	1.05
Acushnet Holdings Corp.	0.88
Moelis & Co.	0.83
UFP Industries Inc.	0.82

TOP FIVE DETRACTORS % Contribution

Atrion Corp.	-0.09
RLI Corp.	-0.01
PriceSmart Inc.	-0.01
Donaldson Co. Inc.	0.12
Jack Henry & Associates Inc.	0.12

% Contribution: Absolute weighted contribution.

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

AVERAGE ANNUAL TOTAL RETURNS (%) as of 12/31/23

	QTD	YTD	1 Year	3 Year	5 Year	10 Year	Since Inception (10/18/96)
Fund Class I	14.49	32.38	32.38	11.96	19.01	14.84	11.29
Index	14.03	16.93	16.93	2.22	9.97	7.16	8.13

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 0.99%.

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 2000® Index** is a market capitalization-weighted index of the 2,000 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 it 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, medium, or large-sized companies may enhance that risk. **Industrial Concentration:** Because the portfolio is presently heavily weighted in the industrial sector, it will be impacted by that sector's performance more than a portfolio with broader sector diversification. **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:** The value of the securities in the portfolio may go up or down in response to the prospects of individual companies and/or general economic conditions. Local, regional, or global events such as war or military conflict, terrorism, pandemic, or recession could impact the portfolio, including hampering the ability of the portfolio's manager(s) to invest its assets as intended. **Prospectus:** For additional information on risks, please see the fund's prospectus.

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