

## Virtus KAR Small-Cap Growth Fund

A: PSGAX (92828N627) | C: PSGCX (92828N619) | I: PXSGX (92828N593)

### MARKET REVIEW

Global equities continued to climb in the fourth quarter of 2017, capping off a year of stellar performance. The broad U.S. equity market, as measured by the S&P 500® Index, returned 6.64% in the quarter, bringing its full-year gain to 21.83%. U.S. small-cap stocks, as measured by the Russell 2000® Index, returned 3.34% for the quarter and 14.65% for the year. Foreign equities, as measured by the MSCI EAFE® Index, posted a gain of 4.23% for the quarter, for a full-year return of 25.03%. Emerging markets stocks, as measured by the MSCI Emerging Markets Index, rose 7.44% in the quarter, helping drive a 37.28% gain for the year, a notable surge following several years of underperformance.

Key factors that pushed markets along into record territory in 2017 included strong corporate earnings, low inflation, and improving optimism for a more pro-business environment, especially with the tax cuts in the U.S. Markets were also broadly characterized by low levels of volatility and minimal performance declines throughout the year.

### PERFORMANCE

The Fund outperformed the benchmark Russell 2000® Growth Index during the quarter, with a return of 7.31% (Class I) versus 4.59% for the benchmark. The portfolio was helped along by strong stock selection in the financial services and technology sectors. Negative stock selection in the consumer discretionary and materials and processing sectors detracted from performance.

Interactive Brokers Group and Copart contributed the most to performance in the quarter.

- > Interactive Brokers, a global electronic brokerage firm, benefited as growth in customer accounts outpaced expectations. The company also has largely completed the exit from its inferior market making business.
- > Copart, which operates an online vehicle auction site, outperformed in the most recent quarter as end-market tailwinds, such as more technologically complex vehicles and auto body shop consolidation, drove salvage volumes higher. Copart's advantaged business model is expected to position the company to capitalize on these positive industry dynamics for many years into the future.

Fox Factory Holding and Emerald Expositions Events detracted the most from performance in the quarter.

- > Fox Factory, which manufactures "ride dynamics" products for mountain bikes and other vehicles, saw a slowdown following atypically high growth rates driven by the initial production and early success of the Ford Raptor pickup truck for which Fox supplies suspension products.
- > Emerald, which operates business-to-business trade shows, underperformed in the fourth quarter due to a couple of negative one-time occurrences at its larger trade shows. We expect these issues to be resolved quickly and believe Emerald's advantaged position in the industry will enable considerable free cash flow generation going forward.

### PORTFOLIO CHANGES

We made no new purchases or complete sales in the portfolio during the quarter.

### OUTLOOK

The outlook for 2018 is favorable overall, but to expect another 2017 would be unreasonable. More volatility and performance drawdowns are anticipated in the year ahead as markets return to more normal conditions. 2018 should continue to provide investors with mid-to-high single-digit equity returns but most likely not without a bumpy ride along the way. Now may be a good time for investors to review their asset allocation and make sure they can "sleep at night" with their current equity exposure. For our part, we will continue to own high-quality businesses with competitive advantages that we believe can shine in good and bad times.

## Virtus KAR Small-Cap Growth Fund

### INVESTMENT ADVISER

Virtus Investment Advisers, Inc.

### INVESTMENT SUBADVISER

Kayne Anderson Rudnick Investment Management, LLC

### INVESTMENT PROFESSIONALS



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



**Todd Beiley, CFA**  
Industry start date: 1999  
Start date with the Fund: 2008

### TOP TEN HOLDINGS

% Fund

Autohome, Inc. Sponsored ADR	8.31
Fox Factory Holding Corp.	5.90
Interactive Brokers Group, Inc.	4.87
Old Dominion Freight Line, Inc.	4.71
Ollie's Bargain Outlet Holdings Inc.	4.55
Copart, Inc.	4.43
MercadoLibre, Inc.	4.32
HEICO Corp.	4.24
Aspen Technology, Inc.	4.22
Rightmove plc	4.09

Holdings 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 6/28/2006
NAV	7.31	36.99	36.99	20.04	20.22	12.79	11.17
Index	4.59	22.17	22.17	10.28	15.21	9.19	9.73

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](http://virtus.com) for performance data current to the most recent month-end.

The fund class gross expense ratio is 1.25%.

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](http://www.virtus.com).

Index: The **Russell 2000® Growth Index** is a market capitalization-weighted index of growth-oriented stocks of the smallest 2,000 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 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.

**Please carefully consider a Fund's investment objectives, risks, charges, and expenses before investing. For this and other information about any Virtus mutual fund, contact your financial representative, call 1-800-243-4361, or visit [virtus.com](http://virtus.com) for a prospectus or summary prospectus. Read it carefully before investing.**

**Not insured by FDIC/NCUSIF or any federal government agency. No bank guarantee. Not a deposit. May lose value.**

Distributed by **VP Distributors, LLC**, member FINRA and subsidiary of Virtus Investment Partners, Inc.

2018 01-18 © 2018 Virtus Mutual Funds