VIRTUS FUNDS

Virtus Newfleet Senior Floating Rate Fund

A: PSFRX (92828R545) | C: PFSRX (92828R537) | I: PSFIX (92828R529) | R6: VRSFX (92828W254)

MARKET OVERVIEW

Bank loans returned 2.52% for 1Q—with almost all of it coupon-driven—as rate cuts failed to materialize in January or March after both CPI and economic data came in hotter than expected. With the Federal Reserve's (Fed) interest rate path proving difficult to predict, the loan market's performance has exceeded expectations thus far. We think bank loans will return 7-8% this year.

The resilient economy also bolstered borrowers' ability to pay down debts; EBITDA growth has ticked up, which means leverage has come down while interest coverage has improved. The downgrade-to-upgrade ratio is also at a five-month low. These strong fundamentals and an attractive coupon have stoked investor appetite for risk. With volumes at $48.8 billion for 1Q, collateralized loan obligation issuance is now at its fastest pace since 4Q21 and marks the fastest start to a year since the Global Financial Crisis. On the retail side, loans recorded inflows for seven consecutive weeks through March 27—a run not seen since April/May 2022.

The flip side of this is that supply has not kept up. While M&A activity picked up toward the tail end of the quarter, overall, leveraged buyouts stayed at low levels during the period. This resulted in prices going up as investors chased a smaller pool of assets. The quarter ended with 38% of the loan market priced at or over par, and borrowers were thus able to refinance and reprice—i.e., reduce interest expense—and push out loan maturities. About 10% of the market repriced at an average savings of about 54 basis points (bps). These savings are material in a high-interest environment where interest coverage, debt service, and interest expense remain a concern.

As loan market investor sentiment improved, private credit deals took the opportunity to shake off higher-cost financing—about $10-11 billion came back into the broadly syndicated loan market to reduce interest expense. This contrasts with last year's trend when $16 billion left the broadly syndicated loan market to go to private credit due to a lack of investor appetite and prohibitively high new-issue spreads.

HOW THE FUND PERFORMED

The Fund (Class I) returned 2.14% for the quarter versus the Credit Suisse Leveraged Loan Index return of 2.52%.

Contributors

> Strong issue selection within cable/wireless video, healthcare, and information technology helped performance.

> Cash holdings also helped performance.

Detractors

> Weak issue selection within the broadcasting, chemicals, gaming/leisure, energy, and services sectors detracted from performance.

> An underweight to CCC/Split CCC-rated loans had a negative impact on performance as risk assets outperformed.

CURRENT FUND STRATEGY

Though we're still underweight risk relative to the market, that gap has started to close over the last nine months as we began to adapt to the reality that the economy was more resilient than previously thought and as recession risk looked increasingly less likely. We're therefore looking to be fully invested while incrementally adding higher-quality risk. Though we're overweight single B-rated loans overall, it would be more accurate to say we're overweight higher-quality Bs and underweight lower-quality Bs. We will probably be keeping this bias in the near term.

Overall, we're adding risk to defensive sectors. We maintain an overweight on sectors exposed to the U.S. consumer, such as gaming/leisure and food. We're also overweight on healthcare. We maintain underweights on the information technology, wirelines, wireless, and cyclical sectors.

OUTLOOK

It's true that current loan market valuations look rich relative to historical levels. However, in an environment where the economy is in better-than-expected shape, rate cut forecasts are pushed further out, borrowers are taking the right measures to manage the cost of borrowing, and the base rate remains attractive, we think there is a strong case to be made for long-term investors to own loans. Even in a scenario where the Fed cuts rates three times this year, the bank loans sector would still be yielding more than high yield because of its 100 bps in yield advantage.

Should investor demand stay healthy—particularly if the Fed skips rate cuts in May—capital markets might be open to riskier single-B borrowers, allowing them to reduce interest expense and, by extension, improve loan market fundamentals at the margins. This is significant, as the issuer quality of lower-rated borrowers poses one of the major potential risks within bank loans. These technical dynamics, refinancings, and borrowers' ability to manage through a higher-rate environment will inform our view on implementation and will be the main areas of focus for us moving forward.

INVESTMENT ADVISER

Virtus Investment Advisers, Inc.

INVESTMENT SUBADVISER

Newfleet Asset Management

PORTFOLIO MANAGERS

David L. Albrycht, CFA
Industry start date: 1985
Start date as Fund Portfolio Manager: 2008

Kyle A. Jennings, CFA
Industry start date: 1992
Start date as Fund Portfolio Manager: 2008

Francesco Ossino
Industry start date: 1996
Start date as Fund Portfolio Manager: 2012

TOP TEN HOLDINGS

	% Fund
Sigma Holdco BV Facility B7, 01/02/2028	1.08
UKG Inc. Term Loan B, 02/10/2031	1.05
Transdigm Inc. Term Loan I, 08/24/2028	1.00
WEC U.S. Holdings Ltd. Initial Term Loan, 01/27/2031	0.99
Applied Systems Inc. Initial Term Loan (2024) (First Lien), 02/24/2031	0.97
Ineos Finance PLC 2027-II Dollar Term Loan, 11/08/2027	0.97
CSC Holdings LLC 2022 Refinancing Term Loan, 01/18/2028	0.93
Peraton Corp. First Lien Term B Loan, 02/01/2028	0.91
Medline Borrower LP Initial Dollar Term Loan, 10/23/2028	0.90
Filtration Group Corp. 2021 Incremental Term Loan, 10/21/2028	0.87

Holdings are subject to change.

AVERAGE ANNUAL TOTAL RETURNS (%) as of 3/31/24

	QTD	YTD	1 Year	3 Year	5 Year	10 Year	Since Inception (01/31/08)
Fund Class I	2.14	2.14	10.87	5.37	4.56	3.73	4.70
Index	2.52	2.52	12.40	5.82	5.30	4.56	4.98

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 0.87%. The net expense ratio is 0.75%, which reflects a contractual expense reimbursement in effect through 1/31/2025.

The net expense ratio minus interest expense on borrowings is 0.65%.

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 **Credit Suisse Leveraged Loan Index** is a market-weighted index that tracks the investable universe of the U.S. dollar denominated leveraged loans. The index is calculated on a total return basis, is unmanaged and not available for direct investment. The unmanaged index returns do not reflect any fees, expenses, or sales charges.

Newfleet Asset Management is a division of Virtus Fixed Income Advisers, LLC ("VFIA"), an SEC registered investment adviser.

Notes on Risk: Credit & Interest: Debt instruments are subject to various risks, including credit and interest rate risk. The issuer of a debt security may fail to make interest and/or principal payments. Values of debt instruments may rise or fall in response to changes in interest rates, and this risk may be enhanced with longer-term maturities. **Bank Loans:** Bank loans may be unsecured or not fully collateralized, may be subject to restrictions on resale, may be less liquid and may trade infrequently on the secondary market. Bank loans settle on a delayed basis; thus, sale proceeds may not be available to meet redemptions for a substantial period of time after the sale of the loan. **High Yield Fixed Income Securities:** There is a greater risk of issuer default, less liquidity, and increased price volatility related to high yield securities than investment grade securities. **Liquidity:** Certain securities may be difficult to sell at a time and price beneficial to the fund. **Leverage:** When a portfolio is leveraged, the value of its securities may be more volatile and all other risks may be compounded. **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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