VIRTUS MUTUAL FUNDS

Virtus Vontobel Foreign Opportunities Fund

A: JVIAX (92828R859) | C: JVICX (92828R842) | I: JVXIX (92828R834) | R6: VFOPX (92828W569)

MARKET REVIEW

International equity markets faced significant pressure in the fourth quarter, as volatility escalated. The MSCI EAFE® Index declined by double-digit percentage points over the quarter, with all sectors posting negative results. Market sentiment alternated between panic and relief during the quarter according to the prevailing direction of news related to trade tensions, monetary tightening, and slowing growth in China and the eurozone. Both the Federal Reserve and European Central Bank reiterated their intent to proceed with unwinding their quantitative easing (QE) programs, which they had begun in the wake of the 2008 financial crisis. This served to fan investor concerns that the end of easy money would usher in weaker economic growth.

PERFORMANCE

During the quarter, the Fund (Class I) returned -10.36%, outperforming the benchmark MSCI EAFE Index, which returned -12.54%. For the year, the Fund (Class I) also outperformed, returning -12.36% versus -13.79% for the Index.

For the quarter, the financials sector was the most significant driver of relative returns, helped by our core Indian financials holdings, HDFC Bank and Housing Development Finance Corp. In keeping with our quality growth investment style, we avoided exposure to highly cyclical areas, such as energy, which was a relative headwind for most of the year, and thus benefited from the sharp decline in oil prices during the fourth quarter. Our healthcare and information technology holdings detracted from relative performance during the quarter.

PORTFOLIO POSITIONING

We initiated new positions in two French-based companies during the quarter: Air Liquide, the second-largest industrial gas supplier in the world, specializing in industrial gases used in heat treatment, plastic production, welding, and other processes, and VINCI, a global industrials company in concessions and construction.

We exited our position in Spanish industrials company Aena, as we lost confidence in its capital allocation strategy. We also sold Allied Irish Bank (AIB Group), British American Tobacco, global mobility technology company Aptiv (in the consumer discretionary sector), and global management consulting firm Accenture (information technology) to invest in better opportunities.

OUTLOOK

A number of factors weighed on international markets in the quarter, including the prospect of rising interest rates, uncertainty around Brexit, anti-establishment parties gaining ground in Europe, and the ongoing trade battle between China and the United States. Markets were pummeled over the quarter, and concerns of a slowdown are becoming harder to avoid.

One of our most important observations heading into 2019 concerns the prospect of further interest rate hikes in the United States, as well as monetary policy tightening in Europe. At a high level, we are seeing the return of a vast flow of savings from emerging markets back into countries that have run very low interest rates over the past decade, such as the United States and Europe. As those rates rise and liquidity exits emerging markets, the price of risk in emerging markets will rise, and funding will be more difficult to achieve in some riskier regions (such as indebted frontier markets).

It is virtually impossible to predict the exact moment when the impact of such factors would trickle down to the fundamentals of businesses. Yet, as long-term managers pursuing quality growth companies—stable franchises with solid fundamentals, durable earnings power, and long-term growth potential—we are mindful of risks throughout the economic cycle, no matter how robust or negative the environment. With this approach, we expect to capture some of the upside when markets rise—but also accept lower relative returns as a form of insurance, so to speak, that could benefit a portfolio with steadier value accumulation through difficult times, which will invariably arrive. During times such as these, some quality growth companies that have been hit amid market turbulence still have durable fundamentals and long-term growth prospects—and we believe our strategy should benefit from a "coiled-spring" effect as the market comes to recognize them.

Importantly, in our view, the 2019 and long-term earnings outlook for our portfolio is solid. Even though absolute returns were down in 2018, the businesses in our portfolio continue to grow profits, which should be the ultimate determinant of stock prices. Additionally, international stocks are trading at a discount to their 15-year average and to the U.S. market. In light of all this, despite the prevailing gloom and doom sentiment among investors, we are starting 2019 on an optimistic note.

Virtus Vontobel Foreign Opportunities Fund

INVESTMENT ADVISER

Virtus Investment Advisers, Inc.

INVESTMENT SUBADVISER

Vontobel Asset Management

PORTFOLIO MANAGERS

Matthew Benkendorf
Industry start date: 1998
Start date with Fund: 2016

Daniel Kranson, CFA
Industry start date: 1999
Start date with Fund: 2016

David Souccar
Industry start date: 1996
Start date with Fund: 2016

TOP TEN HOLDINGS

	% Fund
Unilever NV Cert. of shs	4.85
HDFC Bank Ltd.	4.80
Nestle S.A.	4.48
RELX plc	4.08
Alimentation Couche-Tard Inc. Class B	3.23
Constellation Software Inc.	3.07
Bunzl plc	3.02
Diageo plc	2.84
Heineken NV	2.63
Keyence Corp.	2.61

Holdings are subject to change.

AVERAGE ANNUAL TOTAL RETURNS (%) as of 12/31/18

	QTD	YTD	1 Year	3 Year	5 Year	10 Year	Since Inception 5/15/2006
Fund Class I	-10.36	-12.36	-12.36	3.67	3.40	7.64	4.13
Index	-12.54	-13.79	-13.79	2.87	0.53	6.32	1.95

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 1.12%. The net expense ratio is 1.07%, which reflects a contractual expense reimbursement in effect through 3/31/2021.

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. Class I shares have no sales charges or distribution or service fees, therefore their returns do not reflect these expenses. Fees and expenses vary, and other share classes are subject to sales charges and fees. Class I shares are offered primarily to eligible institutional investors who purchase the minimum amounts required as described in the prospectus and may not be available to all investors. For fund performance on other share classes, please visit www.virtus.com.

Index: The **MSCI EAFE® Index (net)** is a free float-adjusted market capitalization-weighted index that measures developed foreign market equity performance, excluding the U.S. and Canada. The index is calculated on a total return basis with net 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. **Foreign & Emerging Markets:** Investing internationally, especially in emerging markets, involves additional risks such as currency, political, accounting, economic, and market risk. **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.

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