VIRTUS MUTUAL FUNDS

Virtus Vontobel Foreign Opportunities Fund

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

MARKET REVIEW

Volatility continued in the international equity markets through the second quarter. Despite solid economic growth momentum in the U.S., Europe, Japan, and many emerging markets (EM), activity around the globe set the markets toward a risk-off footing. Concerns included the U.S. continuing to lift interest rates on the back of accelerating inflation, a strong U.S. dollar alongside a sell-off in EM currencies, a continued rise in oil prices, and U.S.-initiated trade negotiations appearing set to impose tariffs, with China threatening retaliation.

Energy and healthcare were the only positive sector performers in the MSCI EAFE® Index. The MSCI Europe Index rose 4.0% in euro terms, but because of currency movements, dropped by 1.3% in U.S. dollar terms. Political unrest in Italy and Germany dominated headlines. Emerging markets struggled again, with 11 countries delivering double-digit negative returns in U.S. dollar terms over the quarter. We view higher U.S. rates and trade fears as important drivers behind the EM sell-off.

PERFORMANCE

For the quarter, the Fund (Class I) returned 0.46%, outperforming the benchmark MSCI EAFE Index, which declined 1.24%. We believe the stable and consistent earnings profile of our holdings provided a measure of protection as uncertainty returned to emerging markets.

Relative to the Index, our industrials, information technology, and financials holdings were the strongest contributors to performance, while our consumer staples holdings, specifically in the tobacco space, detracted from relative performance over the quarter.

PORTFOLIO POSITIONING

During the quarter, we purchased U.S.-based Medtronic, a global medical device manufacturer. In financials, we purchased London Stock Exchange, a global markets infrastructure company that owns several attractive assets. In consumer staples, we purchased Netherlands-based Heineken, the second-largest brewer worldwide. In industrials, we added UK-based Bunzl, a specialist distribution company that supplies nonfood consumable products, cleaning supplies, and safety equipment, and Irish-based Kingspan Group, which manufactures insulation panels and boards for the building industry. In utilities, we purchased Power Grid Corporation, the state-controlled main electricity-transmission utility in India.

We sold Japanese real-estate company Daito Trust and French healthcare company Essilor International in order to reallocate capital to better opportunities. We also exited Israeli-based Check Point Software Technologies on guidance that the slowdown that began last year would persist through 2018.

OUTLOOK

Risk and volatility are now impacting the markets, and we expect this to continue. The momentum that drove markets in 2017 is being replaced by a series of macro issues. We have not changed how we manage money, but the market has started to acknowledge several risks.

One of the main market risks now is the resurrection of inflation and interest rates. A favorable U.S. backdrop of low unemployment and lower taxes, mixed with higher oil prices, should create inflationary pressure. Tariffs, too, could put upward pressure on prices. We believe the Federal Reserve will continue to increase rates and to shrink its balance sheet, while the government increases borrowing to pay for the recent tax cuts. These measures should continue to increase currency volatility and potentially pressure asset prices worldwide. We look for companies without much leverage, and in today's rising-rate environment, we are even more discerning on this metric.

In Europe, the European Central Bank is closer to the end of quantitative easing and rate increases may start later next year. Europe also has to deal with a meandering economy, a fragile banking system, and political turmoil. Meanwhile, Brexit remains an open question. These are some of the reasons why Europe may be hardest hit by a global trade war.

The market only recently began to pay attention to escalating trade tensions, where the tail risks have increased. The U.S. and China are still far apart when it comes to such difficult issues as solving intellectual property protection and the ability of U.S. firms to gain access to China without entering into joint ventures.

Given rising risks, the need for downside protection becomes increasingly important. Quality growth companies, especially those less exposed to the macro economy, should protect investors in a downturn, as they have historically. Consumer staples is one industry where we find companies that fit the bill; we find others in certain healthcare areas and even in some industrials. When it comes to investing in companies that provide downside protection, we do not compromise on growth.

Our focus has always been on the resilience of the businesses we own. This discipline is not rewarded in every period. For a while, the market was fixated on companies' current growth, irrespective of sustainability. This year, some risk appreciation is coming back—a healthy development. We believe our quality growth discipline is evergreen and should hold us in good stead in today's market, as it has over the past two decades.

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

TOP TEN HOLDINGS	% Fund
HDFC Bank Limited	4.21
Housing Development Finance Corp. Limited	3.60
Unilever NV Cert. of Shs	3.43
Booking Holdings Inc.	3.35
Mastercard Inc. Class A	3.19
Alimentation Couche-Tard Inc. Class B	2.96
Constellation Software Inc.	2.80
Reckitt Benckiser Group plc	2.80
Paddy Power Betfair plc	2.75
Nestle S.A.	2.59

Holdings are subject to change.

AVERAGE ANNUAL TOTAL RETURNS (%) as of 6/30/18

	QTD	YTD	1 Year	3 Year	5 Year	10 Year	Since Inception 5/15/2006
Fund Class I	0.46	-1.69	6.88	8.01	7.08	4.51	5.30
Index	-1.24	-2.75	6.84	4.90	6.44	2.84	3.05

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 1.17% and reflects the direct and indirect expenses paid by the Fund.

The gross expense ratio minus the indirect expenses incurred by the underlying funds in which the Fund invests is 1.16%.

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.

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