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FOCUS ON: VIRTUS GLOBAL REAL ESTATE SECURITIES FUND

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Adding global real estate to a portfolio offers both growth and diversification benefits. This asset class stands to benefit from the tailwinds of positive global economic growth and minimal new real estate supply. Plus, its returns tend not to move in lock step with other investments. This edition of our "Focus" series makes sense of this less well-known market opportunity.

What is driving the global opportunity in real estate?

The investment opportunity in listed REITs (Real Estate Investment Trusts) is often thought of as primarily U.S.-centric. In reality, the opportunity has become increasingly global, for several reasons: the on-going introduction of REIT-like legislation overseas; lower levels of securitized real estate in many developed countries allowing for faster growth in the asset class; and increased investor demand for these types of securities. Real estate will become the 11th GICS sector this year.

While the REIT structure was first introduced in the U.S. in 1960, today there are approximately 40 countries with approved REIT legislation. We believe the on-going securitization of commercial real estate is a secular trend that will continue to mature and evolve in the coming decades.

The robust growth in the listed real estate markets of Spain, Ireland, and Mexico are just a few recent examples of this trend at work. Investors can gain exposure to key global markets, tenant demand, and the rental cash flow streams from many properties, including where people want to live, work, shop, store, and distribute consumer goods. Moreover, the global listed real estate markets generally provide access to superior quality real estate, aligned management, strong governance, and greater liquidity than is readily available to investors in the global private commercial real estate market.

Why invest in global real estate securities?

An allocation to global real estate may tangibly improve an investor's portfolio by delivering compelling risk-adjusted returns with lower correlations to other investments. Returns stem primarily from exposure to high quality, lease-based cash flow and dividend growth from many different types of commercial real estate, spread across numerous countries.

Generally, the global listed real estate universe offers an attractive, large, and growing list of traded real estate equities, including many mid- and small-cap names which may not be well covered by the Street. This light coverage creates an opportunity to add value through a fundamentally-oriented and rigorous investment process.

The Focus series is a production of Virtus University. To learn more, visit **Virtus.com**, follow us on Twitter **@Virtus**, or call **1-800-243-4361**

Over the last five years, global real estate securities have generated superior risk-adjusted returns compared to traditional global equities. In addition, they have also demonstrated a lower correlation of returns to traditional U.S. equities over the same time period.[1]

What is distinct about your approach to investing in this opportunity?

The global listed real estate universe offers an attractive, large, and growing list of traded real estate equities, including many mid- and small-cap names which may not be well covered by the Street.

Duff & Phelps has long been a pioneer in listed real estate investing. About a decade ago, we were early to recognize that overseas investment opportunities were far more diverse than just U.S.-listed REITs with investments abroad. While some competitors dove into overseas companies focused on for-sale residential development (even though they historically did not invest in U.S. homebuilders), we concluded that the global ex-U.S. investment opportunity should be thematically consistent with the business profile of companies we historically found compelling in the U.S.

We determined that a focus on an investment universe comprised of "rental" real estate companies would be the best approach. These companies are true owner-operators of commercial real estate that generate 70% or more of their revenue from the rents of their underlying investment properties. Historically, they have delivered superior risk-adjusted returns compared to "non-rental" companies and we believe they offer the investment characteristics that investors seek when making an investment allocation to real estate. These characteristics include:

- stable cash flow and dividend growth;
- lower correlation to other asset classes; and
- a degree of inflation protection.

In structuring our research coverage, we recognized there would be many cross-border benefits to having analysts cover both U.S. REITs with property investments in other countries, and global ex-U.S. names abroad. This distinctive approach to research coverage has facilitated true global portfolio construction.

Can you share insights into your investment process and the attributes you look for in the companies included in the portfolio?

A consistent investment philosophy and process underpins our listed real estate strategies, including global securities. In fact, the initial framework was put in place more than two decades ago and has been refined over the years. Our investment process comprises five distinct steps, which build upon one another to ultimately drive the construction of a high-conviction portfolio with explicit risk management guidelines.

Step 1—Identify real estate market and sector opportunities via three dimensions:

- the macro environment
- the real estate space market (supply and demand of rental space utilized by tenants)
- the real estate asset market (the transaction market for real estate property between buyers and sellers)

Our research and analysis of these three areas helps drive our initial considerations and focus for assets by property sector, geographic location, and lease duration, to name a few variables.

Step 2—Delve into and filter the listed investment universe of real estate securities on liquidity and proprietary fundamental and valuation factors.

This step identifies potential investment opportunities and prioritizes our research efforts. Our dynamic proprietary screening process seeks to rank companies on the fundamental and valuation characteristics we believe are key to a potentially attractive investment opportunity and are representative of a growth-at-a-reasonable-price or GARP investment style:

- above average cash flow and dividend growth;
- a strong balance sheet;
- healthy return on invested capital; and
- an attractive relative valuation.

Step 3—Assess a company's intrinsic value.

This is the core of our research process. We thoroughly analyze the companies that rank well through our filtering process across five key areas:

- management analysis
- investment property analysis
- cash flow analysis
- future growth prospects
- our proprietary multi-valuation process (the Duff "MVP")

We are striving to identify companies that have management teams with a strong capital allocation track record and governance, clear strategy, appropriate staffing

[1]Source: Bloomberg. Global Real Estate as measured by the FTSE EPRA/NAREIT Developed Rental Index. Traditional global equities as measured by the MSCI World Index. U.S. equities as measured relative to the Wilshire 5000 Index. Indexes are defined on page 4.
Past performance is not indicative of future results.

levels to implement their strategy, a well-located and competitively positioned real estate portfolio, and a balance sheet that is appropriately structured to support the future growth of the business. Ultimately, we want to invest in companies at prices that we believe are at a discount to the intrinsic value of the business.

Step 4—Portfolio construction with oversight and monitoring by our risk management team.

At this stage, the Portfolio Managers synthesize initial reads on the three dimensions of the real estate market with bottom-up company research. We vet each analyst's recommendation, as well as views of other analysts on the team, before building a portfolio around the highest conviction ideas, taking into account security risks, the Fund's risk management guidelines, and portfolio risk controls. From a risk management perspective, we seek to have a focused, but not too concentrated, portfolio.

> The diversification benefits of this exposure should not be understated. Unlike many other global industries that have been profoundly impacted by the increase in global trade and are greatly influenced by global supply and demand fundamentals, real estate, by and large, remains a local business that is driven by local supply and demand.

Step 5—An exercise of our sell discipline.

While there are many reasons we may choose to sell or trim a security position, the most common are when a security approaches its intrinsic value, a better risk-adjusted opportunity becomes available, a change in the fundamental thesis underlying the investment occurs, or for considerations of investment guidelines and target weights.

Do you hedge foreign currencies?

To date, we have not hedged currencies because we start with the premise that exposure to foreign currencies is one of the desired attributes of a global investment allocation. In our experience, tactical currency hedging is rather difficult. Additionally, active or passive foreign currency hedging can introduce meaningful transaction costs that might detract from long-term returns. Thus, for investors with a medium- to long-term investment horizon, we view that the impact of currency movements will likely be negligible if the global portfolio is well-diversified.

What is your current outlook for the global listed real estate market?

Overall, we view a backdrop of low, but positive, global economic growth and minimal new real estate supply as positive fundamental tailwinds for global listed real estate going forward. Improving global economic growth should facilitate further increases in real estate operating cash flows and dividends through higher property occupancies and, in cases where occupancy has reached equilibrium, higher rents. In effect, higher rents represent pricing power, a hard-to-find attribute in today's investment climate. Combined with the supportive tailwind to real estate asset pricing, our base case is for another positive total return year for global real estate securities in 2016.

The private real estate asset market (the transaction market between buyers and sellers) varies by market and country, but is further along in the cycle in terms of valuations. We believe the global weight of capital looking for a home in high-quality, core real estate is meaningful enough to continue to support current real estate asset pricing. Additional price appreciation may be driven largely by cash flow growth, as opposed to continued cap rate compression. Exceptions could include those countries and markets not as far along in the current real estate cycle. With the significant amount of overseas buyers and private real estate equity capital that has been raised but remains unspent, we expect M&A activity to continue, if not accelerate, during 2016. This theme was evident through the fourth quarter of 2015, particularly in the U.S., as additional privatizations were announced.

An added event this year is worth highlighting. After market close on August 31, 2016, the real estate sector will become the 11th Global Industry Classification System ("GICS") sector. Currently, listed real estate is classified in the financials sector. While the institutional investment community has long considered real estate its own asset class with distinct and positive investment characteristics, we view this step as an important one for listed real estate, and one which we expect should increase investor demand.

To learn more about the Virtus Global Real Estate Securities Fund, contact your financial advisor or visit Virtus.com.

About the Authors:

Geoffrey Dybas, CFA heads Duff & Phelps' Global Real Estate Securities team. He is senior portfolio manager and co-founder of all dedicated REIT strategies managed by Duff & Phelps, including the Virtus Real Estate Securities Fund; Virtus International Real Estate Securities Fund; Virtus Global Real Estate Securities Fund; Virtus Real Estate Securities Series, a series of the Virtus Variable Insurance Trust; the REIT portfolio within the DNP Select Income Fund Inc., a closed-end fund; and separate institutional accounts.

Prior to joining Duff & Phelps in 1995, Mr. Dybas was a corporate banker for Bank One, and began his investment career in 1989.

Mr. Dybas holds a B.S., cum laude, from Marquette University and an M.B.A. from the Kellogg School of Management at Northwestern University. Mr. Dybas is a member of the CFA Institute, the CFA Society of Chicago, the National Association of Real Estate Investment Trusts (NAREIT), and the European Public Real Estate Association (EPRA).

Frank Haggerty, CFA is senior managing director and portfolio manager of the dedicated REIT strategies managed by Duff & Phelps. He is a portfolio manager of the Virtus Real Estate Securities Fund; Virtus International Real Estate Securities Fund; Virtus Global Real Estate Securities Fund; Virtus Real Estate Securities Series, a series of the Virtus Variable Insurance Trust; the REIT portfolio within the DNP Select Income Fund Inc., a closed-end fund; and separate accounts. His primary responsibilities include sharing portfolio management and trading decisions, and conducting research on the equity REIT and international real estate universe.

Prior to joining Duff & Phelps in 2005, Mr. Haggerty was a senior analyst and portfolio manager at ABN AMRO Asset Management for seven years. At ABN AMRO, he was a member of the North American real estate securities team and was responsible for analyzing the residential, office and lodging property sectors. Additionally, Mr. Haggerty was the portfolio manager for the North American region of the ABN AMRO High Income Property Fund (Netherlands-based mutual fund) and several Japanese-based accounts that utilized a similar investment strategy.

Mr. Haggerty began his investment career in 1996. He holds a B.S. from Illinois State University, an M.B.A. from DePaul University Kellstadt Graduate School of Business, and the Chartered Financial Analyst designation. He is a member of the CFA Institute, the CFA Society of Chicago, the National Association of Real Estate Investment Trusts, and the Board of Directors, Illinois State University Educational Investment Fund.

Annual Lipper Fund Awards: The Fund had the highest "Lipper Leader for Consistent Return (Effective Return)" value in its classification for the three-year period. Lipper ranks the Virtus Global Real Estate Fund based on the total return as of 12/31/15. The fund is ranked within a universe of funds similar in portfolio characteristics and capitalization. Rankings do not include the effect of a fund's sales load, if applicable. Lipper ranking is for Class I shares only, other classes may have different performance characteristics.

The **FTSE EPRA NAREIT Developed Rental Index** (net) is a free-float market capitalization-weighted index measuring global real estate securities, which meet minimum size, liquidity and investment focus criteria. The index is a sub-set of the FTSE EPRA NAREIT Investment Focus Index Series, which separates the existing constituents into both Rental and Non-Rental Indices. A company is classified as Rental if the rental revenue from properties is greater than or equal to 70% of total revenue. The classification is based on revenue sources as disclosed in the latest published financial statement. The index is calculated on a total return basis with net dividends reinvested.

The **MSCI World Index** (net) is a free float-adjusted market capitalization-weighted index that is designed to measure the equity market performance of global developed markets. The index is calculated on a total return basis with net dividends reinvested.

The **Wilshire 5000 Total Market Index** is a market capitalization-weighted index composed of more than 6,700 publicly-traded companies that meet the following criteria: are headquartered in the United States, are actively traded on an American stock exchange, and have pricing information that is widely available to the public.

The indexes are unmanaged, their returns do not reflect any fees, expenses, or sales charges, and they are not available for direct investment.

IMPORTANT RISK CONSIDERATIONS

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. **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. **Real Estate:** The fund may be negatively affected by factors specific to the real estate market, including interest rates, leverage, property, and management. **Foreign & Emerging Markets:** Investing internationally, especially in emerging markets, involves additional risks such as currency, political, accounting, economic, and market risk. **Prospectus:** For additional information on risks, please see the fund's prospectus.

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