COM ETF 2021 Year End Review: Will Commodity Trends Persist in 2022?

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Inflation Persisted as Rates Rose

The Federal Reserve's denial throughout most of 2021 that inflation was more persistent, and not transitory, finally gave way toward the end of last year. We experienced some of the highest inflation numbers in 30 years and that was reflected in most commodity prices. Although interest rates rose in 2021, they seem to have more room to run based on their historic relationship with the Consumer Price Index (CPI). We will see if that plays out, but if the early days of 2022 are any indication (interest rates have recently eclipsed pre-pandemic levels), the probability is high that rates will rise. Historically, there has been a high degree of correlation between inflation and subsequent higher commodity prices. This pattern has continued to hold true over the course of the last year.

The Direxion Auspice Broad Commodity Strategy ETF ($COM) was up nearly 28% for 2021*, (click the link for fund standardized returns) which was in line with other notable broadly diversified commodity indices. The commodity benchmarks that are tilted more toward Energy, showed some relative outperformance in 2021, with that sector being the top performer. However, those same indices that are heavily concentrated in Energy were some of the biggest laggards in 2020.

One of the distinguishing characteristics of the COM ETF is that it equal weights a position based on risk, meaning that a commodity with higher volatility will receive a lower initial weighting, while an individual commodity with lower risk characteristics will receive a higher weighting. In addition, the COM ETF, unlike most other notable broad commodity benchmarks, is not always 100% long. Based on price trends, $COM has the ability to be in cash with an individual commodity when it is showing a downward price trend, which can potentially provide a better risk/return profile relative to long-only commodity exposure.

Most of the individual commodity markets that make up the strategy contributed to the outsized gains for the year. In fact, 10 out of the 12 commodities within the portfolio provided positive performance attribution for 2021. The sectors that were the strongest performers were the Energy and Agriculturals/Softs sectors. The Softs include cotton and sugar, which were two of the largest gainers for the Fund outside of Energy. $COM's ability to have meaningful weights in commodities like sugar and cotton differentiate it from most other commodity strategies that do not have that diversification capability. Thus, the performance attribution with the COM ETF can look much different than other broad commodity strategies.

Energy Outperformed

The Energy sector led the way in 2021, as all four of the commodities that make up the sector (Crude, Natural Gas, Heating Oil, and Gasoline) produced gains. The Energy markets were aided by a number of factors that included slow production increases by OPEC+, as well as a pickup in demand caused by the reopening economy due to the advent of vaccines. In addition, clean energy initiatives in the U.S. and around the globe led to further decrease in capital expenditure spending and production cuts in the U.S. The realization that alternative energy sources will take some time to supplement oil and natural gas usage has further contributed to supply constraints. In 2021, both natural gas and crude oil prices saw their highest levels since 2014.

Agriculture Stayed Strong, Metals were Mixed

The Agricultural commodities sector, which includes Grains and Softs, had an overall strong year as well. This sector had lagged over the previous few years but came out swinging in 2021 and collectively produced one of the best years in recent memory.

**The performance data quoted represents past performance. Past performance does not guarantee future results. The investment return and principal value of an investment will fluctuate. An investor's shares, when redeemed, may be worth more or less than their original cost. Current performance may be lower or higher than the performance quoted. For Standardized Fund Performance, click here.*

In the case of Agriculturals, all three grains (corn, wheat, and soybeans) had solid performances. Corn led the way within the sector, as weather-related issues that impeded planting along with U.S. stockpiles dropping to very low levels, in conjunction with a jump in demand (particularly in China) created strong upward price movement. The narrative for corn was a theme that pervaded throughout the overall sector where tightening supplies couldn't keep up with the increase in demand. Some of the supply constraints induced by COVID led to higher prices for cotton and sugar.

The Metals commodities sector had mixed performance in 2021 as the Precious Metals (gold and silver) lagged by finishing negative for the year, while Industrial Metal (copper) had strong returns.

In the case of copper, the Biden administration's "build back better" focus certainly provided a springboard for prices. In addition, China's continued commitment to infrastructure spending was a big positive for the Industrial Metal. Copper is an integral component in the power grid and will continue to be a metal that will be a barometer for the health of the global economy, particularly with China.

The Precious Metals commodity sub-sector had a difficult 2021 as both gold and silver finished down for the year. Our Direxion COM ETF (click link for fund holdings) was in a cash position with gold for the majority of 2021, as we just entered a long position in November. In the case of silver, we have been in cash since August. These are just two examples of how the $COM ETF differentiates itself as a rules-based tactical approach to commodity investing, while most notable peers are always 100% invested regardless of the environment.

Both silver and gold had a rough 2021 for a variety of reasons including the strengthening U.S. Dollar. Historically, the Precious Metals commodity sector tend to be the most sensitive to a stronger U.S. Dollar and that was the case in 2021. When looking at gold and silver, the flight-to-safety aspect of them never really materialized last year, as it was mostly a risk-on environment. In addition, the reemergence of cryptocurrencies, particularly Bitcoin, as a possible digital substitute for gold, took some of the luster off investing in gold. Both gold and silver could potentially rise once again as they are key components in some of the clean energy initiatives including solar panels and circuit boards within electric vehicles, in addition to overall inflation fears.

Where are Commodities Headed in 2022?

As we enter 2022, it appears that price and wage inflation are themes that could pervade for some time to come. Commodities tend to be cyclical in nature and can be long in duration. Some would say we are in the early innings of another commodity super cycle that can have legs for years to come. Certainly the consumer is seeing inflation first hand whether shopping for groceries or filling up their gas tank. Higher commodity prices are touching our everyday lives. If an inflationary environment continues to evolve, one may have to look outside of traditional investments, with asset classes such as commodities, like the $COM ETF strategy, that are able to diversify an overall portfolio.

The Fund is an actively managed ETF that does not seek to replicate the performance of a specified index and is not required to invest in the specific components of its benchmark index. Investing in the Fund may be more volatile than investing in broadly diversified funds. The Fund is not suitable for all investors and should be utilized only by sophisticated investors who understand leverage risk and intend to actively monitor and manage their investment.

Short-term performance, in particular, is not a good indication of the fund's future performance, and an investment should not be made based solely on returns. Because of ongoing market volatility, fund performance may be subject to substantial short-term changes. For additional information, see the fund's prospectus.

Direxion Shares Risks - Through the close of trading on August 30, 2021, COM is an actively managed ETF that does not seek to replicate the performance of a specified index and is not required to invest in the specific components of its benchmark index. Effective August 31, 2021, the ETF will track, before fees and expenses, the performance of the Auspice Broad Commodity Index. An investment in the Fund involves risk, including the possible loss of principal. The Fund is nondiversified and includes risks associated with concentration that results from the Fund's investments in a particular industry, sector, or geographic region which can result in increased volatility. The Fund's use of derivatives such as futures contracts and swaps are subject to market risks that may cause their price to fluctuate over time. Risks of the Fund include risks related to investment in commodity-linked derivatives and commodities, Futures Strategy Risk, Leverage Risk, Market Risk, Natural Disaster/Epidemic and Market Disruption Risk, Counterparty Risk, Cash Transaction Risk, Subsidiary Investment Risk, Interest Rate Risk, and Tax Risk. Please see the summary and full prospectuses for a more complete description of these and other risks of the Fund. Exchange-traded commodity futures contracts generally are volatile and are not suitable for all investors. The value of a commodity-linked derivative investment typically is based upon the price movements of a physical commodity and may be affected by changes in overall market movements, volatility of the index, changes in interest rates, or factors affecting a particular industry or commodity, such as drought, floods, weather, embargoes, tariffs and international economic, political and regulatory developments. Commodity-linked derivatives also may be subject to credit and interest rate risks that in general affect the value of debt securities. The Fund's investments in derivatives may pose risks in addition to, and greater than, those associated with directly investing in securities or other investments. Risks associated with the use of futures contracts are (a) the imperfect correlation between the change in market value of the instruments held by the Fund and the price of the futures contract; (b) possible lack of a liquid secondary market for a futures contract and the resulting inability to close a futures contract when desired; (c) losses caused by unanticipated market movements, which are potentially unlimited; (d) the Adviser's inability to predict correctly the direction of securities prices, interest rates, currency exchange rates and other economic factors; (e) the possibility that the counterparty will default in the performance of its obligations; and (f) if the Fund has insufficient cash, it may have to sell securities or financial instruments from its portfolio to meet daily variation margin requirements, which may lead to the Fund selling securities or financial instruments at a time when it may be disadvantageous to do so.

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