# To Rotate or Not to Rotate; That is the Question...

Throughout this market cycle, nearly all investors have asked themselves this question regarding growth and value...likely too many times to count. So, in this article we will discuss:

- Is a rally in value stocks coming?
- What impact can the COVID Delta Variant have for investors?
- Can the growth rally continue?

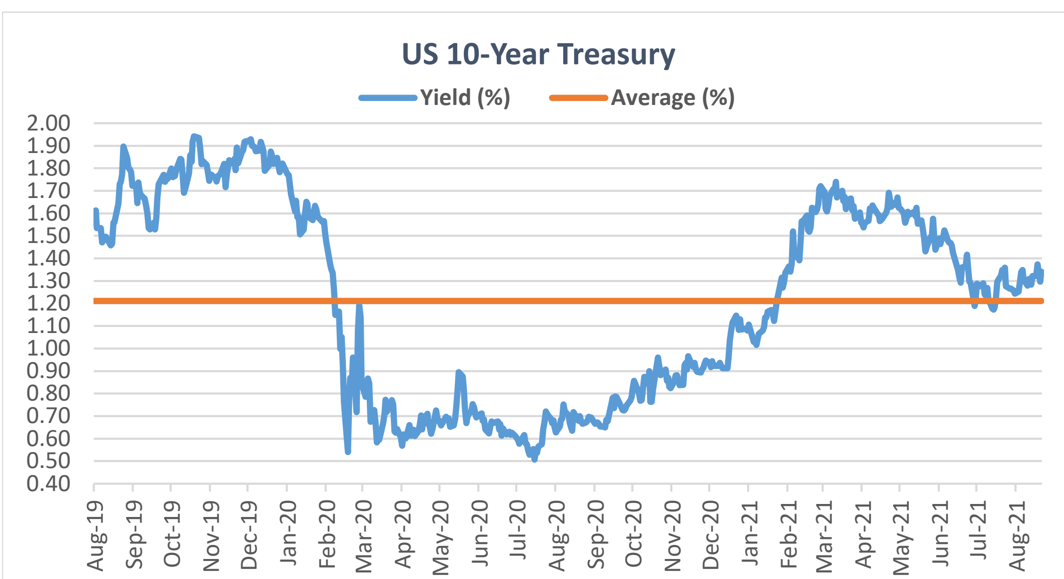
## IS A RALLY IN VALUE STOCKS COMING?

With the U.S. 10-Year Treasury yield potentially forming a double-bottom recently, investors are positioning for another value rally. The numbers confirm this. Year-to-date, investors have allocated over $25.1B in net flows across the seven largest U.S. Large Cap Value ETFs, and have continued to add another $1.9B since the start of August. For comparison, this is almost $5B more in 2021 than in the previous two years, *combined*.

Will this prove, however, to be another false dawn, which sees value stocks outperforming growth for just a short period until it ultimately takes a back seat to growth?

Time will tell, and value likely needs a re-accelerating economy with a steepening yield curve to sustain its outperformance, but investors seem to be positioning for this trend to continue.

### US 10-YEAR TREASURY YIELD MAY HAVE DOUBLE-BOTTOMED




Source: Bloomberg Finance, L.P., as of September 10, 2021.

## WHAT IMPACT CAN THE COVID DELTA VARIANT HAVE FOR INVESTORS?

The most recent value rally coincided with Pfizer's announcement of a successful COVID-19 vaccine. In short, the economy could begin to reopen safely. However, the delta variant has made investors question the path of economic recovery, which has seen coincided with a decrease in yields.

Like past episodes, the answer remains mixed and results may continue to be episodic. The below excerpt from a Spotlight we wrote on April 16, 2020 titled *"When is the Right Time to Buy Value"* may provide context:

> *Many investors have been firmly overweight growth over the last 18 months. Until this month, this has been fruitful as growth outperformed value by almost 15% during that time. While we remain cognizant of the fact that absolute returns remain on the forefront for most investors at this time; more recently, growth has outperformed value by almost 8% during the recent selloff that brought about the fastest-ever bear market.*
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> *Even with the recent end of the 11-year bull market due to the evolving situation regarding the coronavirus, we are not ready to rotate away from growth. So, what would change this? In short, the data will guide us.* ***In other words, we believe that we need to see the start of a new economic cycle in order to overweight value.***
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> *On March 15, along with cutting the federal funds rate to the lower bound, the Federal Reserve announced that they would begin another asset-purchasing program better known as quantitative easing (QE4). This time around, they planned to purchase $500 billion of Treasuries and $200 billion of Mortgage Backed Securities until they upped the ante with the move to unlimited QE across a wider range of securities including investment grade corporate ETFs.*
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> *While this time may prove to be different, previous rounds showed growth outpacing value, and we believe that QE4 will be similar. On average, growth outpaced value by 3.05%. The outperformance of growth during periods of quantitative easing tends to be consistent with yields decreasing across the maturity spectrum and investors seeking out more potential certainty around earnings potential, which growth stocks can provide.*
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> *On the other hand, during the so-called "Operation Twist", the Federal Reserve used the proceeds from short-term assets to purchase longer-term ones. This action lowered the yields on long-term Treasuries and supported economic growth to encourage borrowing. This forced investors to push further out on the risk spectrum, and within the stock market, those names most associated with the greatest level of skepticism around their revenue streams or balance sheet health saw substantial interest.*
>
> *Due to the depth of uncertainty in today's environment, signals are appearing to line up closer to periods of QE as investors will likely continue to hunker down with heightened levels of risk aversion. A key question this time around will be the impact that fiscal stimulus may have on steadying the economy and improving investor appetite. In addition, the Federal Reserve may implement new programs, such as yield curve control that would explicitly target a certain rate of longer-dated bonds. Most importantly, investors will need to see notable improvement in the current coronavirus crisis in order to see steps towards a return to normalcy, whether in the economy or the markets.*
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> *When the green shoots begin to emerge for the start of a new market cycle, it may finally be time for value to shine, as investors will look to embrace those stocks, which have been most out of favor. Of course, the challenge will be timing this, especially when it comes it comes to identifying appropriate leading indicators in a time of significant uncertainty. A simple measure that will likely be top of mind in this case will be financial conditions broadly, as they have recently deteriorated to levels last seen heading into the Global Financial Crisis (GFC). During the GFC, we did begin to see financial conditions start to improve prior to other indicators, such as jobs numbers.*

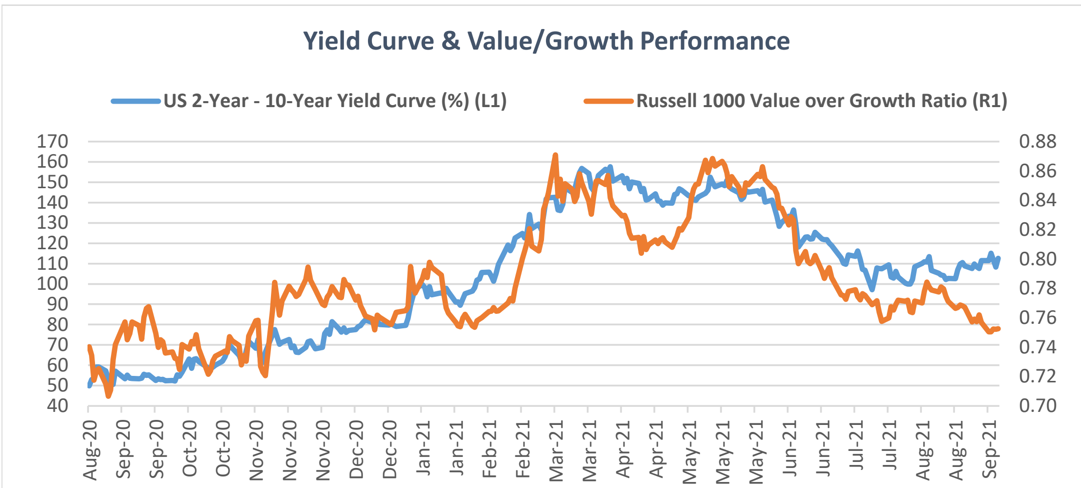
While we bring readers back to 2021, investors should keep in mind that much of this macro backdrop remains relevant. Stocks are looking well beyond 2021, but uncertainty persists. In many ways, a renewed economic cycle has come to fruition, but one lined with a unique recovery in supply-and-demand that has now resulted in scarcity, and there are even whispers of inflation. This, along with other factors, has translated to outcomes in the stock market that investors have not witnessed in some time, such as sustained small cap outperformance and leadership from sectors such as Energy and Financials (especially relative to Technology). With that, we have seen notable outperformance in value stocks relative to growth names.

## CAN THE GROWTH RALLY CONTINUE?

The question we ask ourselves today is: can it continue?

Due to their underlying cyclicality, value stocks are inherently tied to interest rates. Simply put, rates rise when the economy is doing well and expanding, and stocks more exposed to improving financial conditions tend to outperform. When economic growth is scarce, investors seek areas in the market where growth can be found, and premiums tend to be placed on those names, sectors, and industries. Today, the U.S. 10-Year sits well below its 2021 highs of nearly 1.80% and the curve has flattened, but investors who have re-aligned portfolios coming out of the pandemic crisis to be less underweight value (and potentially even overweight it) have benefitted thus far.

### THE YIELD CURVE WILL LIKELY CONTINUE TO DRIVE GROWTH/VALUE PERFORMANCE




Source: Bloomberg Finance, L.P., as of September 10, 2021.

In the interim, leadership will likely remain mixed until greater clarity on the path of the economy recovery comes to bear. Looking forward, we believe that interest rates, and the interest rate curve, will play a crucial role in determining what the next leg for value and growth looks like. While investor flows tell a story of continued support across the value spectrum, some may argue that the recent slowing in economic activity is set to bolster growth stocks. On the other hand, another wave of economic expansion would be significant for value stocks to continue their recent leadership.

### Implementation Ideas

- The Direxion Russell 1000® Growth Over Value ETF [**RWGV**] balances 150% long exposure to the Russell 1000® Growth Index and 50% short exposure to Russell 1000® Value Index.
- The Direxion Russell 1000® Value Over Growth ETF [**RWVG**], which overweights value stocks relative growth stocks.

## Index Descriptions

- **Russell 1000® Growth Index:** The Russell 1000 Growth Index measures the performance of those Russell 1000 companies with higher price-to-book ratios and higher forecasted growth values.
- **Russell 1000® Value Index:** The Russell 1000 Value Index measures the performance of those Russell 1000 companies with lower price-to-book ratios and lower forecasted growth values.

Investments cannot be made in an index. Unmanaged index returns do not reflect any fees, expenses or sales charges. Past performance is no guarantee of future results.

***An investor should carefully consider a Fund's investment objective, risks, charges, and expenses before investing. A Fund's prospectus and summary prospectus contain this and other information about the Direxion Shares. To obtain a Fund's prospectus and summary prospectus call 866-301-9214 or visit our website at direxion.com. A Fund's prospectus and summary prospectus should be read carefully before investing.***

**Value Investing Risk -** Investments in value stocks present the risk that a stock may decline in value or never reach the value the adviser believes is its full market value. In addition, a value investment strategy may go out of favor with investors during certain parts of the market cycle, which may negatively affect the investment's performance.

**Growth Investing Risk -** The prices of growth stocks are based largely on projections of the issuer's future earnings and revenues. If a company's earnings or revenues fall short of expectations, its stock price may fall dramatically. Growth stocks may be volatile and may also be more expensive, relative to their earnings or assets, compared to value or other stocks.

**Distributor:** Foreside Fund Services, LLC.