

# Three Strategies to Address Market Volatility Now.

Volatility is a fact of life in financial markets. Unfortunately, many investors get caught off guard and become unnerved when a seemingly random event—such as a health pandemic or geopolitical conflict—roils markets. For long-term investors, the most damaging potential threat of a major equity market shock is not the volatility itself, but the temptation to abandon the larger strategy out of fear and sell assets at the worst possible time.

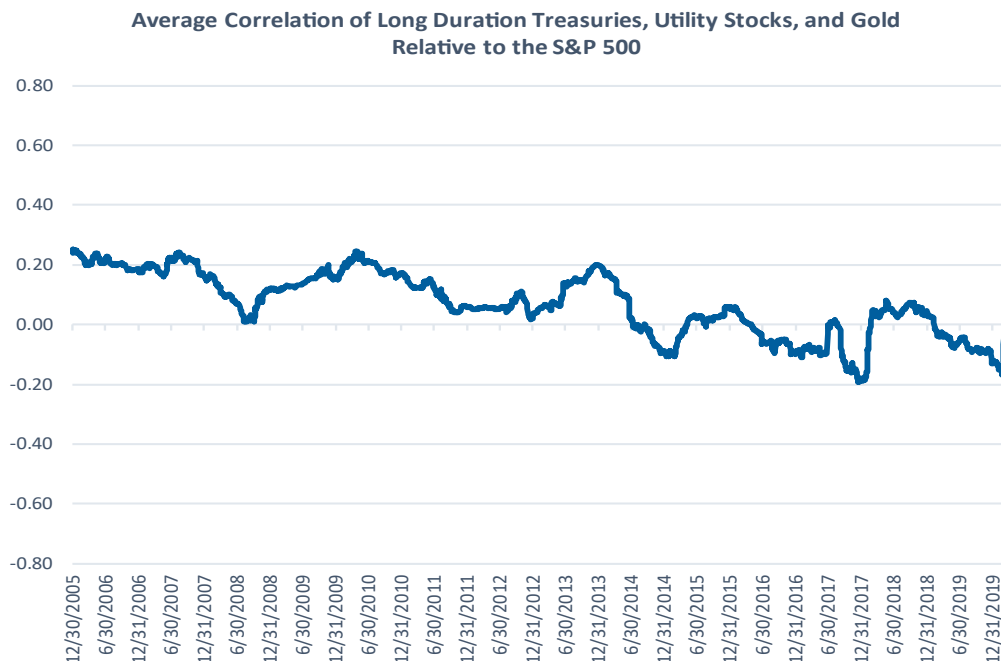
While volatility gives rise to anxiety, it also creates opportunity. Investors who have built volatility-reducing ballast into their portfolios are better positioned to capitalize on the opportunities presented by turbulent market conditions and protect against dips that can undermine long-term performance.

Below, we introduce a range of strategies that long-term investors can use to prepare their portfolios for volatility, depending on the investor's conviction about near-term conditions and longer-term opportunities.

## STRATEGY 1: DIVERSIFY TO STAY INVESTED AND LIMIT DOWNSIDE

Many hedging strategies are only designed to protect portfolios, essentially serving as insurance policies for investors. Such strategies are not designed to keep pace with the market, but instead to pay off only during market drawdowns. While it's certainly better to have an insurance policy in place before your house is on fire, investors may find their behavioral biases taking over if hedges are constantly in the red as markets continue to gain.

Thankfully, other hedging strategies exist which allow investors to participate in market upside while also paying off during flights to safety. One such method is to allocate a portion of portfolio capital to assets that exhibit low historical correlations with equity markets broadly, such as long-term U.S. Treasuries, gold bullion, and utilities stocks. Combined, these assets have an average correlation of zero over the past eight years.



Source: Bloomberg Data 1/4/2010-12/31/2019. Past performance is not indicative of future results. One cannot invest directly in an index. Treasuries represented by the ICE 20+ Years Treasury Index; Utilities represented by the S&P Utilities Select Sector Index; and Gold represented by the spot price of Gold Bullion.

## Gold, Utilities, and Long-Term U.S. Treasurys Have Low Correlation to Stocks

When stocks sell-off sharply, these uncorrelated assets can provide a hedge. Historically, long-term Treasurys and gold generally appreciate during flights to safety, while utilities stocks preserve capital relative to more cyclical sectors. When markets gain, this strategy maintains upside thanks to its stock exposure and also benefits from the steady stream of income provided by Treasurys and utilities stocks.

### Implementation Idea:

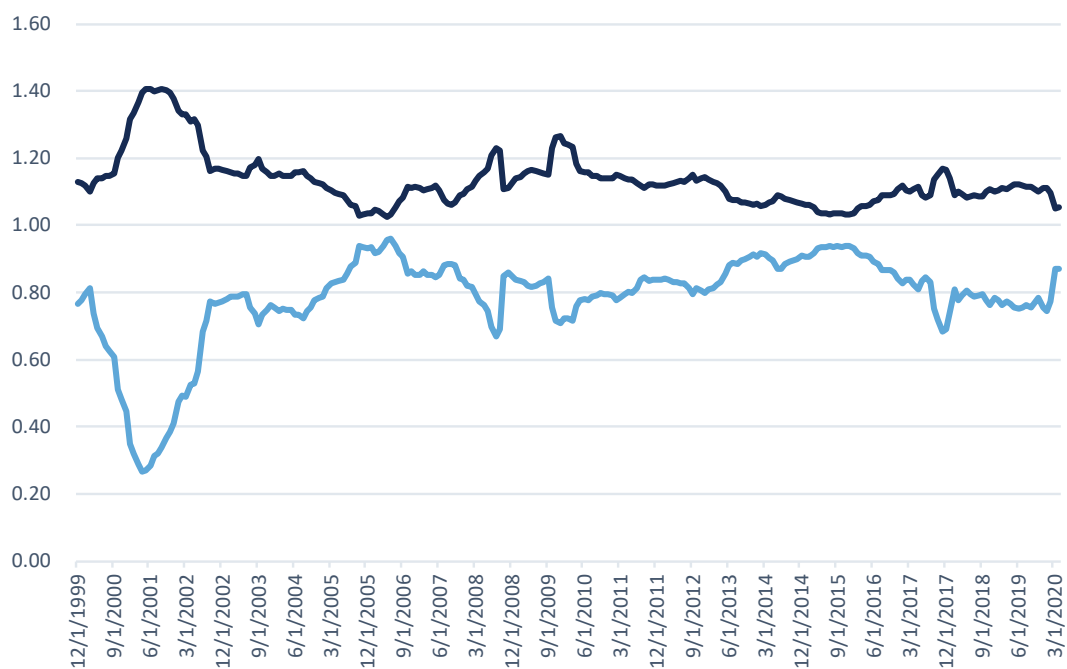
- The [Direxion Flight to Safety Strategy ETF \(FLYT\)](#) provides portfolio diversification through exposure to long-term U.S. Treasury bonds, utilities stocks, and gold bullion. The mix of these low-correlation assets is rebalanced quarterly to ensure the least volatile component has the highest weighting.

## STRATEGY 2: PLAY OFFENSE USING DEFENSIVE ASSETS

Investors who desire to take a more bearish view while continuing to maintain positive exposure to the stock market can reweight their portfolio holdings more defensively, focusing on overweighting sectors that are inherently less sensitive to macro shocks and underweighting, or even selling short, those that are more cyclical. When the economic outlook deteriorates, defensive stocks are likely to outperform cyclical equities based on historical precedent.

In addition to utilities, other defensive sectors such as consumer staples and healthcare stocks exhibit significantly lower historical betas relative to the broader S&P 500. Historical betas (measure of a stock's volatility in relation to the overall market) for all sectors shift over time, but more cyclical ones tend to be greater than 1. Overweighting defensive sectors while underweighting cyclicals helps to retain the upside potential of a rising market while mitigating downside risk.

### Historical Betas Relative to the S&P 500



Source: Bloomberg data 1/1/95-03/30/20. Past performance is not indicative of future results. One cannot invest directly in an index. Cyclical represented by the MSCI USA Cyclical Sectors Index and Defensive represented by the MSCI USA Defensive Sectors Index.

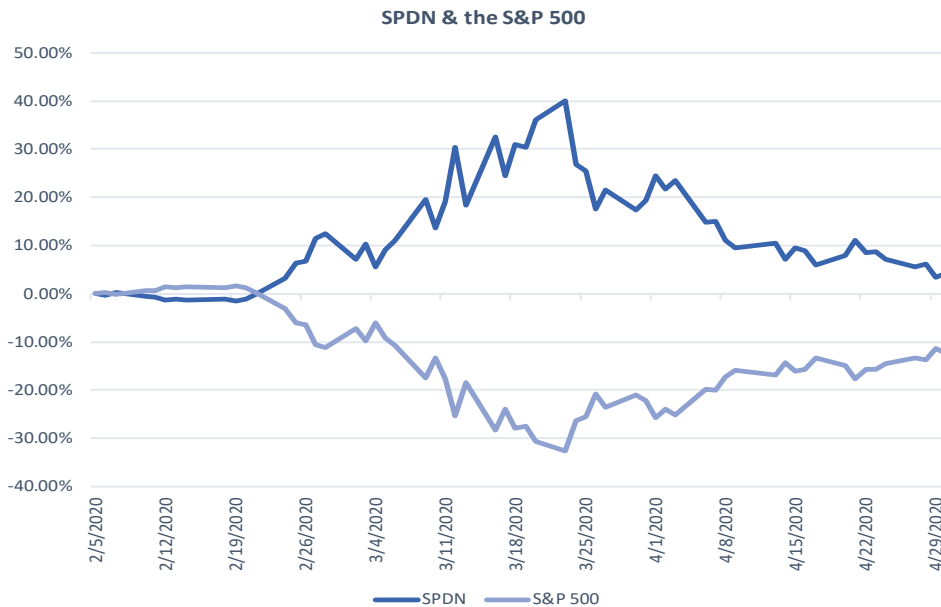
## Historical Beta by Equity Sector

### Implementation Idea:

- The [Direxion MSCI USA Defensives Over Cyclical ETF \(RWDC\)](#) offers investors a way to benefit from the relative performance of defensive versus cyclical stocks. The fund provides 150% long exposure to a basket of healthcare, consumer staples, energy, and utilities stocks, along with a combined 50% short exposure to all other sectors, which are considered to be cyclical ones.

## STRATEGY 3: GET TACTICAL WITH SHORT-TERM SHORTS

For many investors, a more tactical short-term hedge is an attractive tool when facing a more volatile market environment. Investors with long-term conviction in their equity holdings but equally strong short-term concerns can tactically add short exposure in order to gain when markets decline. Tactical shorts can reorient a portfolio's risk exposures quickly without forcing investors to unwind existing long positions.



Source: Bloomberg Data as of 4/30/2020. Past performance is not indicative of future results. Investment return and principal value of an investment will fluctuate so that 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 data quoted. [Click here](#) for standardized performance and month end.

### Implementation Idea:

- The [Direxion Daily S&P 500 Bear 1X Shares ETF \(SPDN\)](#) seeks investment returns, before fees and expenses, of 100% the inverse of the performance of the S&P 500 Index for a single day. Relative to Direxion's more highly leveraged 3X products, SPDN allows investors to tactically add a hedge while allowing more room for error if markets do not correct as expected. It is important to note that the fund should not be expected to provide 100% of the inverse of the benchmark's cumulative returns for periods longer than one day. And investors should understand the risks associated with the use of shorting and are willing to monitor their portfolios frequently.

## Putting It All Together: Participate and Protect

Over the long term, volatility is a natural aspect of equity markets. But over the short term, it is random, largely unpredictable, and episodic. For investors with a long-term horizon, the overall goal should be to build portfolios that can participate in the opportunities presented by evolving market conditions while hedging against the shocks that can unnerve investors and undermine long-term performance.

***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 866-476-7523 or visit our website at [direxion.com](http://direxion.com). A Fund's prospectus and summary prospectus should be read carefully before investing.***

Shares of the Direxion Shares are bought and sold at market price (not NAV) and are not individually redeemed from a Fund. Market Price returns are based upon the midpoint of the bid/ask spread at 4:00 pm EST (when NAV is normally calculated) and do not represent the returns you would receive if you traded shares at other times. Brokerage commissions will reduce returns. Fund returns assume that dividends and capital gains distributions have been reinvested in the Fund at NAV. Some performance results reflect expense reimbursements or recoupments and fee waivers in effect during certain periods shown. Absent these reimbursements or recoupments and fee waivers, results would have been less favorable.

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The Fund described herein is indexed to an MSCI Index. The Fund or securities referred to herein are not sponsored, endorsed, or promoted by MSCI, and MSCI bears no liability with respect to any such funds or securities or any index on which funds or securities are based. The Prospectus contains a more detailed description of the limited relationship MSCI has with Rafferty and any related funds.

**FLYT** - 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.

**FLYT Risks** - An investment in the Fund involves risk, including the possible loss of principal. There are risks associated with the Fund's investment in gold, U.S. treasury bonds, and utility stocks. The value of gold has historically experienced extended periods of flat or declining prices in addition to sharp fluctuations, which may result in significant volatility and potential losses to the Fund. A security backed by the U.S. Treasury or the full faith and credit of the United States is guaranteed only as to the timely payment of interest and principal when held to maturity. The market prices for such securities are not guaranteed and will fluctuate. Utility companies are affected by supply and demand, operating costs, government regulation, environmental factors, liabilities for environmental damage and general liabilities, and rate caps or rate changes. Additional risks of the Fund include, but are not limited to Commodity-Linked Derivatives Risk, Counterparty Risk, Cash Transaction Risk, Other Investment Companies (including ETFs) 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.

**Direxion Relative Weight ETFs Risks** - Investing involves risk including possible loss of principal. The Fund's investments in derivatives may pose risks in addition to, and greater than, those associated with directly investing in or shorting securities or other investments. Cyclical stocks tend to rise and fall with the business cycle and are typically companies that provide consumer discretionary goods or services. Defensive stocks tend to remain stable during various phases of the business cycle due to constant demand for products. Defensive stocks generally include utility and consumer staples companies that produce goods bought out of necessity. There is no guarantee that the returns on the Fund's long or short positions will produce high, or even positive returns and the Fund could lose money if either or both of the Fund's long and short positions produce negative returns. Please see the summary and full prospectuses for a more complete description of these and other risks of the Fund.

**Direxion Shares Risks** - An investment in the ETFs involves risk, including the possible loss of principal. The ETFs are non-diversified and include risks associated with concentration that results from an ETF's investments in a particular industry or sector which can increase volatility. The use of derivatives such as futures contracts and swaps are subject to market risks that may cause their price to fluctuate over time. The ETFs do not attempt to, and should not be expected to, provide returns which are a multiple of the return of their respective index for periods other than a single day. For other risks including leverage, correlation, daily compounding, market volatility and risks specific to an industry or sector, please read the prospectus.

**Distributor for Direxion Shares:** Foreside Fund Services, LLC.