



Todd Dilatush on structured products



Todd Dilatush, Head of Distribution at SCG Asset Management (SCGAM), talks about structured products — their beginnings and the current marketplace — and how his firm adds value to the product set as a fiduciary. For instance, SCGAM manages a repurposed, interval fund that actively manages a portfolio of structured notes: The Alternative Strategies Income Fund, a listed closed-end interval fund with the Nasdaq ticker symbols LTAFX (Class A), LTCFX (Class B), and LTIFX (Class I).

Dilatush also discusses macro trends in the economy, and talks more generally about the work of SCGAM, which specializes in the development and management of advanced derivative-based solutions, capitalizing on market opportunities, and creating customer exposure through rigorous, proprietary analytical modeling, qualitative analysis, and prudent risk management.

Find [here](#) the video interview.

Jane King: Todd Dilatush is currently head of distribution at SCG Asset Management, the company specializes in development and management of advanced derivative-based solutions, capitalizing on market opportunities and creating customer exposure through proprietary analytical modeling, qualitative analysis, and prudent risk management.

Prior to joining SCGAM, Todd spent four years as director of national sales for Luma Financial Technologies, an independent market leading multi-issuer structured products and annuities platform, and he was responsible for soliciting and developing strong client relationships by providing financial technology solutions or structured product distributors including private banks, broker dealers, and independent advisors. He has a bachelor's degree from Lehigh University in mechanical engineering and a master's and MBA from Rutgers.

So welcome, Todd. Great to have you here, and look forward to talking to you about what you do and how you see the economy right now.

Todd Dilatush: Sure, thanks Jane. Again, thank you so much for having me today. So I'm head of distribution at SCG Asset Management, we are an entity of a family office which is Sachs Capital Group. Sachs Capital Group was founded by a gentleman named Greg Sachs. Greg made his name in the industry launching his own hedge fund called Deerfield Capital, which he sold in the late 2000s. I joined SCG Asset Management with some former colleagues of mine to build that distribution and to expand alternative products for the organization.

Jane King: So let's talk about the structured product market.

Todd Dilatush: Sure.

Jane King: How has that evolved? What are some recent developments?

Todd Dilatush: Okay. Well, for good or bad I've been involved in the structured product marketplace for about 20 years now. I'll give you a brief background on the genesis of the product set, from where it began in the US to where we are today, and how that ties into what we're focused on at SCG Asset Management.

So structured products became available really in the US market in the late nineties, initially through private banks offered to ultra-high net worth individuals. A structured note is a hybrid security, these are bonds issued by banks tied to the performance of a referenced asset, and for the context of this conversation, tied to equities, whether they be single stocks, ETFs or indices. So in the early 2000s, the private banks really made a move to go, what I call open architecture, where they allowed third-party product providers to make their products available in the private bank networks.

Once that happened, in that same time period the products started to come readily available in the broker-dealer channels, the independent broker-dealer channels, et cetera. So over the course of time the market has slowly grown, not only in structured notes but also in defined-outcome ETFs, which have been in the media quite a bit, as well as RILAs and FIAs which are a derivative-based insurance product. So that market in total is about \$300 billion in 2023, we expect about 20% year-over-year growth once we get to the end of 2024, so there's a lot of eyes on the product set.

In 2015 or so, the product set really started to take hold in a lot of these distribution channels, and what's unique about structured notes, these are bonds, each bond has a QCIP, and when we think about distribution we're talking about tens of thousands of notes being issued per year. So if you're a user of the products, you could potentially amass a portfolio of 50 to 100 unique structured notes. But these typically sit outside of a typical portfolio allocations while advisors categorize them as alts, you can have a tremendous amount of these QCIPs, very difficult to manage.

In 2015 or so, the technology really kind of took hold to help advisors better manage these positions of structured notes, so that technology advancement has really helped with the broader use case of these structured products. Structured notes are typically used to dampen risk in a portfolio, there's many different payout profiles that you can embed in a structured note whether it's principal-protected or principal-at-risk, but generally speaking they're broken into two categories, either

growth or income. We at SCG Asset Management focus on income-oriented structured products, which I'll get to in a moment.

So the fintech evolution was really one of the big enhancements in the structured product market for a number of years, not much had happened until then. What we're starting to see now is in the last five years or so the implementation of defined-outcome ETFs, they've gone from zero to let's say \$30 billion in assets in five years, but at the same time the structured note market has grown as well, so I would argue that the ETF market is not competing for those same assets that are going into notes. The acceptance of the ETFs I believe are advisors that historically did not want to transact in the note space because they're difficult to hold, they're a very operational intensive product set to manage.

The ETFs are welcome, it's a welcome enhancement into the product set. What we've done at SCG Asset Management is kind of added to the enhancement of the product set as a fiduciary. We've repurposed a legacy interval fund where the strategy is an actively managed portfolio of structured notes. The notes that we utilize in our portfolio are issued by 16 different banks, each note is tied to a single stock, and that's one key difference here with what we're focused on versus what the broader market of structured products are focused on is single stocks as referenced assets.

We have a team of quants where we surface the investable universe per se to optimize note selection and manage them as a portfolio in a wrapped solution. So we see an opportunity there, and we're trying to solve for a gap in the market per se.

Jane King: Okay, thank you so much for that comprehensive history and explanation. It's just always fascinating to me, I cover stocks and companies, to hear all the other financial instruments that are out there. Would you say that your clients are more institutional or are they individual investors?

Todd Dilatush: That's a great question. This is a retail product but our client base is really independent RAAs that tend to custody at Schwab, Fidelity, Pershing, et cetera. Many of which are ex-wirehouse or ex-private bank advisors who are using the product there and look at this as a more efficient vehicle given its wrap solution.

Jane King: Okay, interesting. What are some macro trends you're keeping an eye on? I feel like we've got an election and there's talk maybe of a recession and geopolitical issues, what kind of things do you watch?

Todd Dilatush: Well, in respect to actively managing this portfolio, we really focus on market volatility. So structured products, the income, the conditional income generated in a structured note, and again we have a portfolio of up to 50 unique notes, is really driven by market volatility, but the volatility in that particular security that we tie to. So we look at volatility across sectors, we also look at general volatility on an index basis, and we're also looking at interest rates.

Again, this is senior unsecured debt, these are bonds issued by banks, and clearly bonds do have rate risk. The average duration of this portfolio is very short, it's less than 12 months, which makes it unique when compared to, let's say a more traditional bond portfolio, but I would say those are

the key factors that we look at. And given that we lean on our algorithm that we call “The Selector”, we tend to move over different sectors and different industries based on opportunistic spots in the market.

I’ll just give you an example. If there is a large selloff in, let’s say Tesla, volatility elevates in Tesla and if our models and our portfolio managers are looking at Tesla as a name that can complement the existing portfolio, we might put that trade on in the form of a structured note given its elevated volatility at that point in time because that generates a higher conditional coupon in that bond. So take that on a macro level, we’re doing that across industries and sectors.

Jane King: Okay, interesting, and always fascinating how interest rates are like the lifeblood of all markets. They have such an impact.

Todd Dilatush: For good or bad, yeah.

Jane King: That’s right. So last question, Todd, you mentioned fintech and algorithms, what role is technology playing in what you do?

Todd Dilatush: Technology for us specifically, I mentioned the evolution of the fintechs where an advisor can sign on one of these platforms to help them better manage a portfolio of individual notes. In essence, we’ve kind of created our own platform within the fund itself, where we’re managing all the life cycle events of a structured note; proximity to barriers, call notifications, redemptions, et cetera. So we lean on technology heavily, not only using our algorithm to optimize note selection but to actively manage the portfolio itself. I would argue that it would have been extremely difficult to bring a product like this to market five years ago.

Jane King: Okay.

Todd Dilatush: So it’s helping us manage this fund, it’s helping the structured product industry in general, and technology is welcome.

Jane King: Yeah, Todd, thank you so much for your insight today.

Todd Dilatush: Thank you so much.

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