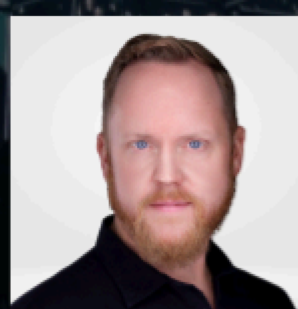
diffusetap
Virtual Event Series

Hybrid Digital Asset & TradFi Products

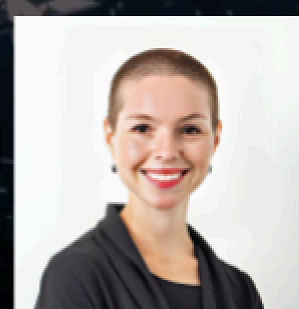
Guest Speaker:

Cato Felán III
Managing Partner
La Hoja Capital Partners

Hosts:



Kenny Estes
CEO & Founder
Diffuse



Ayla Kremb
COO & Co-Founder
Diffuse

DiffuseTap: Hybrid Digital Asset & TradFi Products

Last time on DiffuseTap, Cato Felán III, Managing Partner at La Hoja Capital Partners, talked to us about innovative products that are blending traditional finance and digital assets, why these products could be the catalyst for crypto's mass adoption, and the quintessential problem that crypto is solving in Latin America.

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DiffuseTap

This networking session is part of our weekly virtual events series. Networking (you'll bump into at least a dozen high caliber fund managers) meets purposeful (you'll tap into brand-new sources of ideas)… straight from your armchair like a boss.

Meet the Speaker

CATO FELÁN III is a seasoned investment professional and the Managing Partner of La Hoja Capital Partners, where he spearheads strategies, investments, and investor relations. With over 20 years of experience in asset management, Cato has championed Latin American market initiatives, raising over $10 billion across various financial instruments.

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About Diffuse®

We are an alternative fund platform offering differentiated investment products. From digital assets to VC funds and beyond, we identify green field investment opportunities we feel will have market beating returns and turn them into professionally managed funds. For more information, visit www.diffusefunds.com.

KENNY ESTES: Cato, first off, thank you for joining us. Do you want to tell the good folks a little bit about your background and what you're up to over at La Hoja?

CATO FELAN III: Sure. Thanks, Kenny, and thanks everyone for joining me today. I'm also joined by my co-founder, Meredith Yarbrough, who is on the call as well. We make up La Hoja Capital Partners. I have spent almost 30 years in financial services inside and around Latin America, and dealing with Latin American investors investing in US and global products.

At La Hoja Capital Partners, we curate a portfolio of partnerships, fund managers, and alternative investments, and we bring that portfolio to our Latin American investor base. We also create innovative financial solutions that allow our Latin American investors to invest in US and global products in a streamlined and tax-efficient way.

We believe our portfolio represents the cutting edge of what is going on in traditional finance and digital assets, and we sit at that intersection. I would love to talk about some of the things that we see within and outside our portfolio, and to share about what's going on in the world.

I come from an ETF background. I was one of the early folks at iShares many, many years ago. And dealing with the Latin American investor base, it is something that has worked out very well. We wanted to use that structure to bridge the gap between private funds and public securities, and allow non-US investors to get in.

And as we see in the spot Bitcoin ETF, if you give people something that they're familiar with in a structure and a process, that makes it very streamlined for them to invest in esoteric and unique assets, they gravitate towards it. Those ETFs have become the fastest growing ETFs in history.

And so, we wanted to use that same ethos and that same structure to blend public and private, and allow our non-US investors to invest in these spaces and distribute these private funds at scale. So, when we did that, that process allowed us to get more deeply into the digital space, with tokenization and other types of securitization.

We have had lots of inquiries to tokenize our own note, and what we've done there. We are engaged with a number of players around the world, blazing the path on doing that securitization and tokenization. I'm intrigued to see what is going on with BlackRock, and what their securitization of their funds is going to look like as well.

And then part of our portfolio as well is searching for that blend of traditional finance and digital assets and using the best of both worlds to create a better portfolio. One of the firms out there that is doing something great and innovative is Battery Finance out of Philadelphia. They built a private credit fund, which is a traditional private credit fund, but also has the collateral of the real assets of the underlying investment, plus a sleeve of Bitcoin, around 10-15% of Bitcoin, inside that portfolio as collateral.

What that allows is the private credit side to be much more conservative. If we look at what is going on in private credit around the world, with interest rates so high, private credit managers are using more leverage. They're going more into lower quality assets to boost yield. With this portfolio, the manager can maintain a very conservative profile, not do any distressed lending, and allow the Bitcoin side to really increase the returns in a non-correlated way to the underlying portfolio.

That was one of the portfolios that we were really interested in. We created an exchange traded note for that, which is Irish-domiciled and trades on the Swiss and Austrian exchanges. That has been the impetus of us getting further into that space.

What we find is, and this goes for Latin America (I'm based in Mexico City right now), it is a very different feel here for anything crypto, digital, web3, and blockchain than it feels like in the US. They're solving real problems here for people. And there are so many people. There are 20 to 21 million plus in Mexico City, and another 25 or 27 million in Sao Paulo. So, if you have something that works for a penny, and you do it at scale, it just really seems to grow.

We're seeing lots of firms, like Fuse Capital out of Brazil. They were the first to tokenize their own private fund. They also did the token for another Brazilian crypto company. They did the coin for them years ago. This year, they've been on the forefront of delivering on getting their Brazilian investors into these types of products in a way that is streamlined and efficient for them, and that doesn't pressure them into opening a bank account or creating their own wallet.

It's just really a streamlined way for them to move money. What we're seeing down here in Latin America is that kind of innovation that is continually pushing the envelope, and that is really blending and leapfrogging some of the technologies that were here before.

In Latin America, before, there was landline utilization that was widespread. Then, cell phones took over and had a 90% plus coverage rate. That is what is happening now with remittance payments. We had that talk last week or two weeks ago about one of the firms here doing some remittance payments for those.

That has happened, and it's real in Latin America. There is more money coming into and out of Mexico to the rest of Latin America than there is from the US into Mexico, which has always been a very large amount. But the challenge for a lot of these folks is that there is no conversion rate that you can go to get from a Quetzal to a Mexican peso. You have to go to the US dollar, and then come back to peso.

That is inefficient. It's centralized. There are a lot of commissions there. And so, there are folks that are building up different blockchains like Ultron and facilitating payments like that. Folks that are using the Lightning Network, like IBEX out of El Salvador, who are using the lightning system and the platform to move capital in a very efficient way.

These are just some of the areas that folks in Latin America are doing, and there is a real appetite for it. There is a real appetite for that kind of growth and that kind of experience. It's just a different feel. I have been to a number of web3 and blockchain conferences here, and the predominant theme seems to be that there is a lack of banking access in Latin America. That is why there has been such a surge in fintechs in this space.

And so, when these new types of products come out, people gravitate toward them. They gravitate towards the apps and the structures that allow them to blend their world into the real world, whether they're a business owner sending payments from Mexico to Guatemala, or if they're a Colombian investor who wants to invest in US real estate and using USDT or USDC to do that.

There are lots of different ways that people are blending these traditional finance ways with crypto to facilitate their lives. It's not like in the US, where we have this unicorn-spotting view as to what we're trying to do in this space. It's all real world here in Latin America, and that blend of traditional finance and digital assets is very comfortable for a lot of these investors. They're not worried about it here.

KENNY: Thank you for the intro on what you're up to. We will try to get to the Q&A portion of it. There was a lot of information there. Fun fact, the IBEX guys have been DiffuseTap speakers in the past, so if anybody is interested more about their story, which was a lot of the right place, right time sort of thing, you can hear it on our little Spotify channel.

Obviously, with your background in iShares, you probably have a more informed view on the recent IBIT, commonly referred to as Blackrock ETF. How does that specifically get viewed by international investors? Is that a net good thing, or a bad thing? Is it yet another in the sea of ETFs, like the one you mentioned, the Brazilian ETF for Bitcoin spot? There are a lot of Swiss ETFs that accomplish the same thing too. Or do people really see this as a massive game changer?

CATO: I think people see it as a massive game changer. But I also have a different view on those kinds of specific types of ETFs because it puts pressure on the investor and on the front end, the RIA, the broker, and the private banker to really help them manage that. And right now, a lot of those trades are still coming in unsolicited. It's the investor that is driving that, and they want to buy a lot of it.

It also makes it very easy for them to do so. But what it does is it just creates some friction between what the asset allocation and the overall portfolio for that person is, and what they desire as far as getting more access to Bitcoin in their portfolio.

There is still that kind of friction. There is no cohesive and integrated investment strategy of how to integrate this. It really has been driven by the individual investors that are calling up their advisors, or brokers and bankers, and saying “Hey, I want a million dollars of the IBIT.” That's what I see now.

KENNY: When you say that, is it more at the portfolio construction? Where there are no advisors going out there and telling their clients, “You should have 1, 2, 3% of your assets in this asset class?”

CATO: Yeah, that's still just starting. And with the larger firms, because it's still unsolicited and it's not on the platforms, the investor has to make that call. The advisors and portfolio managers are not calling their clients and saying, “Hey, we are going to add this sleeve of Bitcoin in this way, because it's going to help us do this or do that in the portfolio.”

It's still driven by investor demand and access. It's wonderful that they have it, but it's also not integrated into the overall portfolio, and trying to understand what the intention of the portfolio is when you add that in.

One other thing to think about for international investors is the structure of Bitcoin ETFs. All of them are different from regular exchange traded funds. So, the taxation is going to be different for investors when they sell those things.

They are going to have to do a real good look-through to understand the overall structure. There are adverse tax consequences for them. I'm not giving tax advice. I just know that from seeing the structure of the ETF, it will have some adverse tax consequences for different people in different places if they do not really look into that.

KENNY: Interesting. Can you expand on that? Obviously, we don't want to give tax advice. But this isn't as simple as just “pay cap gains”. It's more complex.

CATO: It's different from the cap gains, because they will have cap gains at the security level. But the underlying structure will create some different things, just like master limited partnerships did and ETFs that had MLPs in there. There are different types of structures that create different tax structures and tax implications for people.

KENNY: Okay, that makes sense. Buyer beware, I guess. And I'm guessing that's part of what you tell your international clients. Larry Fink is going on CNBC. He's talking about how awesome Bitcoin is. Obviously, he has a very vested interest in that conversation. And I have to imagine that they're putting a lot of money into changing those advisors and wealth managers that you referenced earlier, and they’re trying to change their mind and make crypto just a natural place to advise clients to put some of their capital into.

Are you starting to see that Titanic turn? That was a terrible analogy, but are you starting to see people change how they're viewing crypto, like advisors, wealth managers, and institutions?

CATO: I think so. In the US, I've seen that there are some large RIAS that have made some big allocations and are educating their own investors about Bitcoin. Here in Latin America, it's really those who were already Bitcoin-savvy or Bitcoin-adjacent, and friends of Bitcoin who are adding those to the portfolios. But I don't see it as widespread yet. It's still being driven by the individual investors that wanted to get access. And now, this gives them easy access to have it.

KENNY: Okay, I suppose that makes sense. We'll change it a little bit from the actual products for a sec. Where is the US in the crypto landscape, from a regulatory and from an innovation standpoint? I mean, we touch on this a lot, but where do you think we are? Are we so far behind that we can't make it back up, or is there a way forward?

CATO: I think there is always a way forward in the US. There is that rugged individualist and entrepreneurial spirit to push those through. But without the regulatory policies and the advocacy to continue to do that, Latin America and anywhere outside the US is just moving faster. There's more innovation, it's quicker, and it's faster to do newer things. And they're blending that digital asset and traditional finance world.

There are firms in Brazil that are providing loans to US farms based on staking assets in crypto. There are just some different things that people are doing in different ways in Latin America that you just can't do in the US. I also feel like in the US, we are trying to find a problem to solve. But in Latin America, there are so many problems to solve that people are just going at them.

KENNY: Expand on that. Is the argument that in the US, the financial services system is just so damn efficient that Bitcoin and crypto don't necessarily add that much value? Whereas, in Latin America, you have currency issues and all these other problems where Bitcoin is actually solving an immediate issue?

CATO: I think what Blackrock is doing is really showing that, from a portfolio management level, from an investment manager level, from the portfolio construction, portfolio risk and management, and all of those things, there are ways to incorporate digital and crypto into that. For instance, to deliver a better investment experience for an investor through spot Bitcoin ETFs, or to create better access through tokenization.

They've done some of those partnerships with JP Morgan with some of the swaps that they do as well. That is on an infrastructure level, where it is more pervasive on the US side. BlackRock and others are driving the combining of those systems, values, and structures in a way that makes a stronger and better product, solution, or experience for the investors that they have.

Where in Latin America, it's really ground up. It's like, "Hey, I need to send Quetzal to the US, or Mexico, or Brazil. How do I do that, and how do I do it efficiently so it doesn't take me 10 days, and so I don't have to pay 6% commission on it?" There are lots of little things like that. It's a different level. The US is coming in from a 30,000 foot level and bringing it down. And Latin America is ground up, solving the problems that the individuals have here.

KENNY: Okay, so this sounds a little bit like tech debt. You have this massive behemoth, and here is the thing that might make it better. The US approach is “let's try to just gradually integrate them”, as opposed to in LatAm where it’s just like “eh, screw it. We're just going to start from scratch and find out what is the most efficient one”.

CATO: Yeah. I mean, most people still do not have bank access. Full banking access is still very low. The percentage is still very low throughout Latin America. So these types of products that come through apps, which are allowing people to do remittances, payments, and other types of things through crypto and digital, are growing rapidly. They're growing absolutely exponentially, and they're moving super fast and different from what is happening in the US.

KENNY: That makes sense. On that note, actually, you mentioned Lightning with the IBEX guys in El Salvador. Jake wants to know a little bit more about that. What are the fees? For people doing these point-of-sale transactions on the Lightning Network, using one of these things in El Salvador, how does that compare to just regular interchange fees that you get here in the US?

CATO: Yeah, interchange fees are generally about 3 to 6%. On the Lightning Network, I talked to these guys yesterday, and it's about 10 to 15 basis points now. It's a much different proposition, and it's almost instantaneous. I think it’s about 10 minutes to get from one place to the other.

And again, it solves that problem of getting the exchange from a currency that does not normally have a pairing that the bigger clearing houses would do. And so, whether you're doing a Quetzal or anything like that to one other country in Latin America, those are two exchanges you would have to do normally in the traditional finance world.

But in crypto, it's instantaneous. It passes through and it doesn't have those commissions in it. That's growing. That continues to expand, and they're trying to find different ways and different folks to use it, whether it's a Guatemalan builder paying their construction workers in Mexico, or things like that. There are just different ways to use those products and make them seamless and efficient for people that don't have banks, and for people who do not have a place to send a wire transfer.

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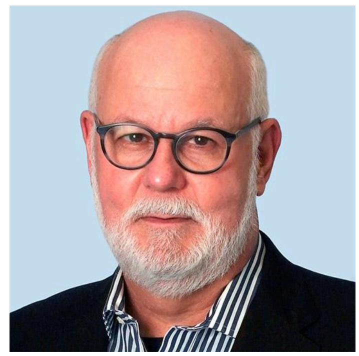

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