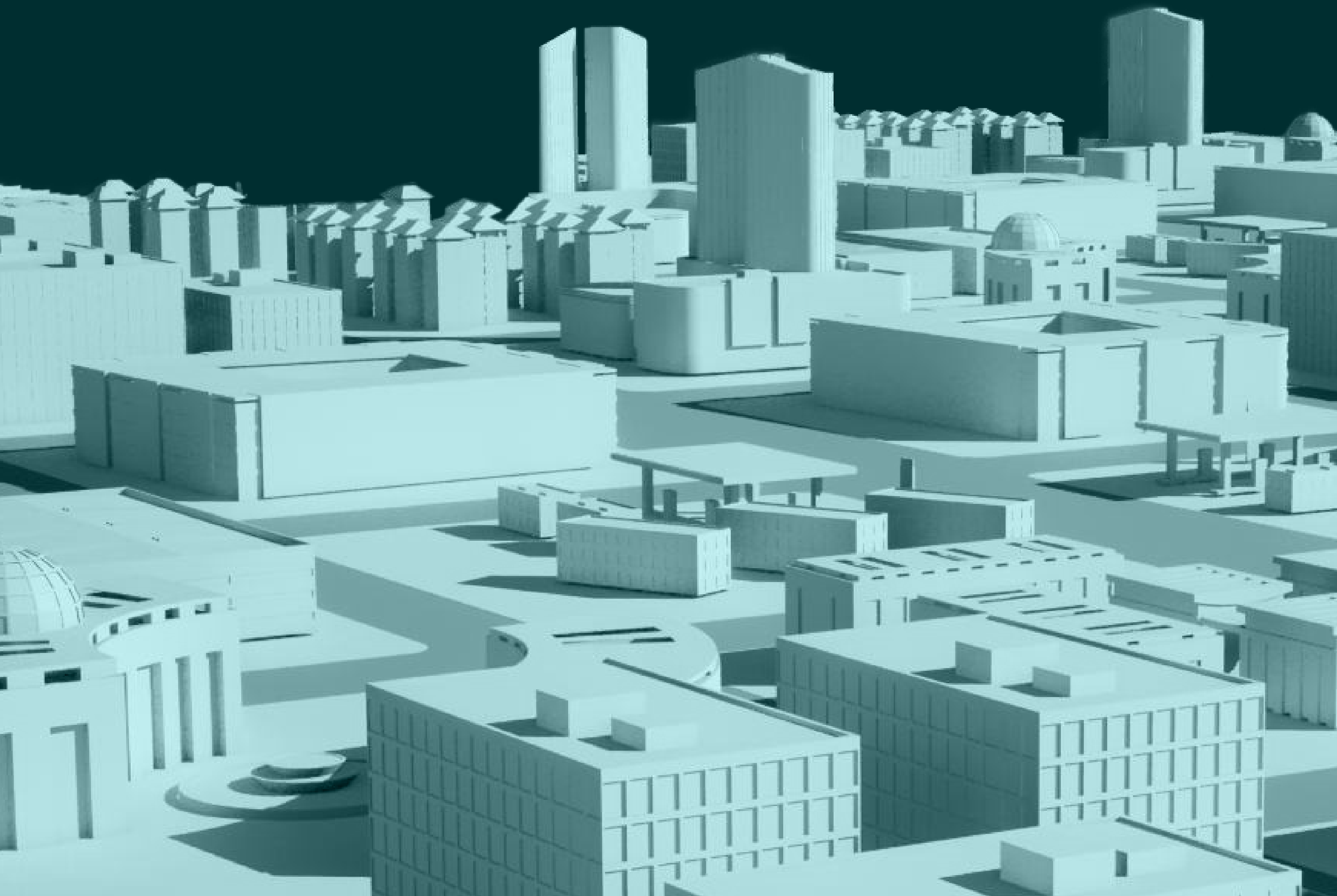
Yieldstreet

Growth & Income REIT

Q1 2024 Commentary



As of March 31, 2024, the Growth & Income REIT has made six investments: three equity investments in multi-family assets, one equity investment in an industrial complex, and two first mortgage debt investments in (i) an office building on a long-term lease to a publicly-traded investment grade tenant and (ii) a newly constructed retail property.

With the start of the new year, the commercial real estate (CRE) community seemed ready to regain stability and return to a more normalized market. The Federal Reserve had indicated potential interest rate cuts in 2024, with three cuts anticipated. However, inflation has remained higher than desired, and the job market remains strong. By the end of the first quarter, the likelihood and timing of any interest rate cuts became uncertain. The initial optimism turned negative, and for a significant portion of the CRE market, transaction activity remains sluggish.

It is clear that the vast majority of transactions, especially equity, that closed between late-2020 and early-2023 are going to be a very challenged. The increase in benchmark rates has resulted in lower property values. Either due to an over leveraged capital stack as a result of lower property values or loan maturities, the ability to inject new capital to extend runway is eroding. We are seeing this trend in the CRE market with the increasing number of defaulted loans, UCC (uniform commercial code) foreclosures, and increasing bank loan loss reserves.

However, some of the most renowned CRE investment firms in the world are calling a bottom and deploying large amounts of capital. Blackstone announced their $10B purchase of a publicly traded apartment REIT. Brookfield, another large CRE investment manager, recently closed their first multi-family acquisition for the first time in two years. While it is positive to see this movement, the vast majority of the market is unable to find levels where buyers and sellers will transact. There are a number of forced sellers who have no other option but to move on due to the issues called out here.

We want to be clear that it is our belief that some of the best investment opportunities of the past 15 years will present themselves in the near term, but one needs to couple that with the challenges that existing deals are going to experience.

Portfolio updates

Atlanta Multi-Family Equity

Atlanta represents the smallest equity investment in the REIT. As we have highlighted in prior quarterly updates, the property is not generating sufficient cash flow to service the monthly interest payments. As of February 2024, the first mortgage loan is in payment default. We do not believe injecting additional equity into the asset under the current capital structure is advisable. We proposed a loan modification to the lender earlier in the year. While we were hopeful that constructive conversations would ensue, no constructive feedback was forthcoming. We received a default notice under the GP loan guarantee from the lender. Rather than pursuing the property as the first source of repayment, the lender is pursuing our GP partner under the failure to replenish the interest reserve. We want to call out that no Yieldstreet entity is a signatory to the guarantee and we have no exposure here. The property did see some positive leasing trends in the 1Q 2024. The Sponsor replaced the property manager with a strong candidate from a separate property in their portfolio. Since taking over the position, the property has seen an uptick in leasing and was 84% occupied at the end of March 2024 compared to just 78% at the end of 2023. Rents however, continue to trend negatively and have decreased by ~1.5% over the same timeframe. The Atlanta rental market continues to be challenged with new supply with vacancy sitting at 17% and rental growth of negative 5.5%. The equity value is materially impaired and given the stance of the lender and their pursuit under the guaranty, the path to recovering any of the equity is not clear.

Tucson Multi-Family Equity

The property continued its positive occupancy and rent trends in the first quarter of 2024, increasing both compared to the end of 2023. At this point, the property is performing in-line or better than the market comp set, however, it is performing materially below the sponsor's original projections for the same time period due to lower rent growth in the market. Currently, the property is not generating enough monthly revenue to cover its monthly debt service payments and funds that were expected to be used for unit renovations are now being used to cover these operating shortfalls. The senior loan matures in April of 2025 and the property will not meet the extension criteria. At this time, it is unclear whether the senior lender will modify the loan or if the JV will need to find another solution, which may entail injecting significant capital to extend the loan and continue improving property operations for an eventual sale.

Portfolio updates (continued)

Norfolk Industrial Complex	As of the end of Q1, the properties were 73% leased. This is a decline from previous quarters, as three tenants vacated the portfolio in September 2023, including one due to a tenant bankruptcy. All vacant spaces are being actively marketed. As a result of the marketing effort, the property has received an LOI for ~14,000 SF, and the Sponsor is currently in lease negotiations with that prospective tenant. The property's Q1 net operating income was ~10% above the revised 2024 budget (which accounts for the current heightened vacancy level), which was driven primarily by lower than expected utility usage and contingency funds for snow plowing and general maintenance that have been utilized. The Sponsor's focus remains leasing up the vacant space at market rents. As a reminder, the Sponsor's business plan is to re-lease or re-tenant a significant portion of the property to triple-net (NNN) lease terms to reduce the operating expense burden and increase net income. The fixed-rate period of the mortgage financing expires in May 2025, at which time the loan will migrate to a floating rate priced at 1-month SOFR + 350 bps. We will continue to evaluate our various options as this date approaches including a potential sale, refinance, or interest rate cap purchase. Until we have additional clarity, we will be mindful of maintaining a strong cash position.
Dallas Multi-Family Equity	The property maintained average occupancy of 94% in 1Q24, which was in-line with last quarter's performance. Rent growth has slowed over the last quarters and was not material in any direction during the first quarter. To date, the sponsor renovated 175 units with an average rent premium of ~$140 per unit. While the property continues to perform well compared to its market comp set, the in place rent is behind the sponsor's underwriting projection at this point in time. The sponsor is focused over the next year to increase rents and operating income at the property to meet original projections. The property's first mortgage loan matures in December 2024 and the property will not meet the extension criteria. The sponsor has been actively engaged with the lender on a waiver of the test, which would allow us to qualify for the extension. A replacement interest rate cap will need to be purchased, which will require an additional infusion of capital to fund.
Tucson Office	The property continues to be 100% occupied by a publicly-traded investment grade tenant. The tenant continues to make timely payments and interest has been received each month since closing. To date, none of the CapEx or tenant improvement funds have been requested by the borrower and remain with Yieldstreet.
Scottsdale Retail	As of Q1 2024, the Property has increased occupancy from ~42% at closing to 59% after two additional tenants, who had signed leases prior to closing, moved in during Q4. The property remains ~80% leased. Yieldstreet has funded three draws since closing, as construction on the pad site continues as planned. Interest has been received on time monthly since closing.

Market outlook

The fourth quarter saw continued muted transaction volume and with the possibility of interest rates being higher for longer, we do not expect an uptick in transaction volume in the first half of 2024. The capital markets continue to be volatile with accretive financing generally available only for top quality real estate projects and borrowers. We also expect losses in the banking sector due to decreased real estate values. Even though charge-offs will be spread over a couple years, some banks will have limited appetite to invest in real estate which we believe will provide opportunities for debt funds and non-bank lenders to take advantage of high interest rates and more attractive valuation of assets throughout 2024.

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