



Investor Newsletter

OCTOBER 2022



Executive Summary

Thank you for your investment in the Socotra Fund and the Socotra Opportunity Fund. This newsletter intends to inform you of recent fund performance and update you regarding our investment outlook. This newsletter is not to be used for risk management or to serve as an investor prospectus.

The Socotra Fund and the Socotra Opportunity Fund returned between 7 percent and 10 percent respectively over the trailing twelve month (TTM) period. Both funds' investment portfolios are exceptionally healthy, having invested in high-quality loans, with high collection rates, and the lowest loan-to-values in our industry. Our strategy entails using zero leverage and adhering to strict underwriting standards.



If you are considering an investment in real estate debt, please contact us.



2208 29th St, Suite 100, Sacramento,
CA 95817 | (855) 889-7626 | socotracapital.com



SOCOTRA FUND

The Socotra Fund's trailing twelve-month (TTM) yield is 7.2 percent and the TTM rate of return was 7.5 percent for reinvestment partners. The projected rate of return for 2022 is ~7.0-7.5 percent. These expectations are subject to change given market conditions.

The Socotra Fund prioritizes the preservation of principal and consistency of income by investing in low loan-to-value opportunities with significant cash (or equity) at risk. Please contact us if you are considering an investment in the Socotra Fund.

OPPORTUNITY FUND

The Socotra Opportunity Fund's trailing twelve-month (TTM) yield is 9.3 percent and the rate of return was 9.7 percent for reinvestment partners. The projected rate of return for 2022 is ~8.5-9.5 percent. The Opportunity Fund redemption window is open from October to December.

The Socotra Opportunity Fund prioritizes maximizing risk-adjusted returns, willing to forgo liquidity and consistency to achieve those goals. It focuses on the acquisition of high-interest loans, discounted notes, and undervalued real estate. Please get in touch with us if you are considering an investment in the Socotra Opportunity Fund.





The Socotra Fund

94.2%
PORTFOLIO CURRENT

50.2%
LOAN-TO-VALUE

7.2%
TTM RATE OF RETURN

7.5%
TTM YIELD

PORTFOLIO METRICS

239 First Lien
OF LOANS

\$920,000
AVERAGE LOAN SIZE

0
31-90-DAY
DELINQUENT LOANS

7
90+ DAY DELINQUENT
LOANS/REO

\$3.4 M
EXPECTED CREDIT
LOSS RESERVE

CASH FLOWS COMMENTARY

COLLECTIONS:

In Q3 2022, the Socotra Fund collected \$34.8M in interest payments and loan payoffs. At the end of Q3, seven loans were non-performing for more than 31 days which includes one real estate-owned property (REO). Of the six nonperforming loans, three are in active foreclosure with auctions scheduled between the next 45-120 days. The remaining three loans are party to bankruptcy proceedings. We anticipate at the conclusion of the bankruptcy proceedings a full recovery of principal. The average loan-to-value for non-performing loans is ~55 percent.

We anticipate the tightening credit environment and the slowing real estate market will induce more loans into default. While this may temporarily reduce collection rates, the investor yield is protected by the low loan-to-value, zero leverage, and ample reserves. In the long run, this should lead to higher yields.

DISTRIBUTIONS AND DISBURSEMENTS:

The fund made \$4.1M in distributions, ~\$1.7M was reinvested, and the other ~\$2.4M was disbursed to income investors.

FUNDINGS, ADDITIONS. AND WITHDRAWALS:

The fund closed on ~\$37.8M in new loans during Q3 2022. The fund added \$13.8M in new investor capital and processed \$4.7M in investor withdrawals. Redemptions are processed on a quarterly basis, and the Socotra Fund is not presently "Gated".

*As of Sep. 30, 2022, weighted by loan amount

SOCOTRA FUND: PORTFOLIO COMMENTARY

The Socotra Fund ended Q3 2022 holding a cash and loan portfolio of ~\$241.3M. The portfolio remains healthy with ~94.2 percent of the portfolio current and an aggregate loan-to-value (LTV) of 50.0 percent. The portfolio is presently allocated ~72 percent to commercial properties and 19 percent to residential properties, while 9 percent is presently held in cash. The fund's largest loan is ~2.7 percent of total capital, indicating no loan concentrations exist. The average term remaining on the portfolio is ~16 months. Near term, there are ~\$32M in loans maturing within the next 90 days and ~\$72M maturing within six months. The Socotra Fund's long-term goal is to deliver consistent monthly income by investing in high-quality real estate loans with low loan-to-value ratios.

INVESTOR YIELD THROUGH SEPT 2022

PERFORMANCE	1 YEAR	3 YEAR	5 YEAR	SINCE INCEPTION
Average Annual Yield	7.2%	7.4%	7.6%	8.5%
Average Annual Rate of Return	7.5%	7.6%	7.9%	8.8%



The Socotra Fund's long-term goal is to deliver consistent monthly income by investing in high-quality real estate loans with low loan-to-value ratios.



The Socotra Opportunity Fund

95.7%
PORTFOLIO CURRENT

48.7%
LOAN-TO-VALUE

9.0%
TTM RATE OF RETURN

9.4%
TTM YIELD

PORTFOLIO METRICS

62 Senior, 6 Junior
OF 1ST LIEN LOANS

\$685,000
AVERAGE LOAN SIZE

1
31-90-DAY
DELINQUENT LOANS

2
90+ DAY DELINQUENT
LOANS/REO

\$608 K
EXPECTED CREDIT
LOSS RESERVE

CASH FLOWS COMMENTARY

COLLECTIONS:

In Q3 2022, the Socotra Opportunity Fund collected \$4.4M in interest payments and loan payoffs. At the end of Q3, three loans were delinquent for more than 31 days which includes one real estate-owned property (REO). One of the nonperforming loans is in active foreclosure, and we expect to have an auction scheduled within the next ~120 days. The other loan is subject to a bankruptcy proceeding. The average loan-to-value for non-performing loans is ~55 percent.

We expect the deteriorating economic environment will push more loans into default. The Opportunity Fund tolerates scenarios that have higher chances of default than the Socotra Fund. These defaults and foreclosures are what generate a higher rate of return, but also can make the Opportunity Fund less liquid, thus requiring more patient capital.

DISTRIBUTIONS AND DISBURSEMENTS:

The fund made ~\$770K in distributions, ~\$370K was reinvested, and the other ~\$400K was disbursed to income investors.

FUNDINGS, ADDITIONS, AND WITHDRAWALS:

The fund closed on ~\$18.5M in new loans during Q3 2022. The fund added \$10.9M in new investor capital. Redemptions are processed annually during Q4 each year.

*As of Sep. 30, 2022, weighted by loan amount

OPPORTUNITY FUND: PORTFOLIO COMMENTARY

The Socotra Opportunity Fund (SOF) ended Q3 2022 holding a cash and loan portfolio of ~\$46M. The SOF seeks scenarios with long-term upside, foregoing a consistent monthly return for longer-term gains. The portfolio contains ~58 percent commercial real estate loans, ~42 percent residential loans, and less than 1 percent cash. The average term remaining in the portfolio is approximately thirteen months. Near term, there are ~\$10.5M in loans maturing within the next 90 days and ~\$19.7M maturing within the next six months. The SOF seeks unique opportunities, such as high-interest loans, distressed notes at favorable discounts, or the acquisition of real estate below fair market value. The SOF expects to stop accepting new capital once it acquires a material concentration of these more difficult-to-value assets at attractive entry points. Given the current economic climate, we anticipate the percentage of non-performing loans to increase which will prompt the closure of the SOF to new capital partners. Closing the SOF is to prevent the dilution of returns to the members who acquired the non-performing loans and preserve the potential upside in default interest or gains on foreclosure.

INVESTOR YIELD THROUGH SEPT 2022

PERFORMANCE	1 YEAR	3 YEAR	5 YEAR	SINCE INCEPTION
Average Annual Yield	9.0%	8.6%	8.5%	8.8%
Average Annual Rate of Return	9.4%	8.9%	8.9%	9.2%



The Socotra Opportunity Fund's long-term goal is to maximize the risk adjusted return. It will forego monthly consistency in exchange for higher returns in the long run.



Loan of the Quarter



\$2,700,000 REFINANCE OF A 54,000 SQFT, 85 UNIT MULTIFAMILY PROPERTY IN AMARILLO, TX

TRANSACTION SUMMARY

The borrower acquired the property in 2014 for \$2.0M and has since spent ~\$1.0M+ in improvements. The property is currently only 70% occupied, and the borrower intends to use their equity to make additional improvements to the property, raise rents, and then sell the property.

Coincidentally, our team previously evaluated this property via a purchase transaction, where the buyer intended to use Socotra for their purchase money loan. As a consequence, Socotra had already done a significant amount of due diligence on the subject property, but that transaction ultimately fizzled. Once the property fell out of contract, the "seller" came to Socotra Capital for the refinance and we were able to close in under two weeks time.

Loan Amount	\$2,700,000
Interest Rate	9.99%
Loan-to-Value	50%
Term	24-Month
Property	Multifamily



MATT YU

LOANS AND INVESTMENTS

Graduating from the University of California, Davis with degrees in economics and biochemistry, Matthew Yu is an excellent problem solver, cleverly crafting fixes for unique scenarios.

A loan originator since 2013, Matt concentrates on the California Bay Area and Seattle, Washington markets. Matt grew up in San Francisco, enjoys fishing as often as possible, playing his drum set, and is happily married to his high school sweetheart.



Market Update

Capital markets continued to struggle under the mounting pressure of the Federal Reserve's rate hikes. [October's jobs report](#) highlights an expanding jobs market with the lowest unemployment rate since before the global COVID pandemic. The number of new jobs added to the economy is still growing, albeit at a slower pace. Recent [inflation data](#) continues to indicate prices grew at a rate that exceeds the Fed's long-term targets. Consequently, the Federal Reserve signaled to the market that it intends to add another rate hike in their latest "[dot plot](#)", suggesting a stabilized Federal Funds rate of 4.0-4.5 percent. Investors fear that the speed and scale of Fed rate hikes are likely to induce a recession, and the Fed has embraced that position by signaling its projected unemployment rate to likely rise in 2023 to 4.5 percent. Any hopes of a potential Fed "pivot" have all but waned entirely so long as inflation persists and the job market remains strong.

Market observers are expecting the residential real estate market to endure the brunt of the Fed's hawkish rate hikes. While values have begun to decline, the pace and magnitude have been modest to date on account of constrained supply propping up valuations. During the global financial crisis, consumer home loans ultimately proved to be toxic assets as defaults spiked. Additionally, there was an overabundance of newer builds and values consequently fell. Comparatively today, home loan delinquencies are near some of the lowest ever recorded, which is partly attributable to the fact that over 90%+ of home loans are on a fixed rate basis, whereas adjustable rate mortgages dominated the market fifteen years ago. Additionally, homeowners are in a position where they hold significant accumulated equity along with favorable interest rates in their current homes. The cost to move is considerable when factoring in current mortgage rates and current home prices. All of this leads to constrained supply, which is evident by the fact that fewer listings are coming to market, [down almost 20% for this same time last year](#).

MARKET UPDATES CONTINUED

Commercial real estate values are also showing declines on account of rising capitalization rates, softening corporate earnings, and capital market conditions. The degree of the impact depends on the asset class, but almost every category has experienced a recalibration.

The most recent FDIC "[Quarterly Banking Profile](#)" highlights banks finished Q2 with one of their largest quarters ever adding new loan balances, while simultaneously seeing a precipitous reduction in bank deposits over that same period. At the time of this newsletter, we are still awaiting industry-wide data for Q3, but the consensus expectations are that loan balance growth is likely to stabilize and provisions for loan-loss reserves are likely to grow based upon how some larger bank earnings are reported. Bank consolidation continues to unfold across the industry, with community banks declining most precipitously. The banking industry's consolidation coupled with the rising rate environment is likely to leave more borrowers underserved by both conventional banks and private lenders alike.



Private lending has proven to be a durable, non-correlated, high-yielding asset class when underwritten and invested with strict discipline.

Amid these ever-changing market dynamics, our commitment to the same strategy is now more important than ever. Private real estate lending can be valuable to any investor's portfolio. Private lending has proven to be a durable, non-correlated, high-yielding asset class when underwritten and invested with strict discipline. At Socotra Capital, we originate loans with low loan-to-value ratios, significant borrower cash at risk, and invest our capital without any leverage.

As the market headwinds begin to weigh on the industry, we expect this strategy to allow our investment vehicles to navigate out of non-performing loans quicker or generate considerable upside over the long run. Investors seeking an uncorrelated and yielding investment, private real estate lending has proven to be durable when the appropriate underwriting is applied.