SFG
Seattle Funding Group

The Source™

Winter 2012 SEATTLE FUNDING GROUP

Leading the Field

As we start 2012, we are beginning to see progress on many fronts, primarily SFG Income Fund's portfolio performance as well as value stabilization in certain submarkets and market segments. We went from collapsing financial markets, rising borrower default percentages and tremendous uncertainty, to a more stabilized portfolio with marked improvement in our non-performing asset percentage. The prognosis remains guarded but improving when combined with an influx of new loans, underwritten at today's valuations, in markets that are beginning to rebound. The SFG Income Funds are weathering the storm, heading in the right direction and investors continue to receive positive returns. In our analysis of the fund's direction, we studied the statistics of not only the prior year, but the last three years, to generate a wider scope and capture data from when we started making the necessary adjustments to our strategies to counter the dramatic economic changes

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In This Issue

that had and were continuing to develop. The view from this broader perspective was interesting and led to the questions, "what if the loans originated during the peak of the real estate bubble (2006 and 2007) were not on the books?; What if we analyzed the portfolio performance more narrowly over the last three years?" We recognize this is hypothetical and, of course, our primary objective as fund managers is to dispose of these 2006-2007 assets and reemploy the capital in new loans at today's valuations. Nevertheless, the results of this analysis were and are interesting to note and prove the effectiveness of our business and lending models going forward. It also confirms our ability to serve the mortgage and real estate community long into the future and is a key component to carving through the challenges we all face today. To achieve this directional clarity, we created some general portfolio statistics for loans originated over the last three years (October 2008 through October 2011). We thought you might find this as interesting and encouraging as we did.

Total loans funded

(October 2008 – October 2011)

We experienced a 68% drop in loan volume from 2008 to 2009 as the markets drew to a near halt. The substantial reduction was predicated by market shock from the sudden economic collapse, compounded by our self-imposed, greatly heightened underwriting standards. The last thing we wanted in the fund, regardless of how much equity supported the loan, was a borrower who might not pay on time. We have accomplished this objective. Today our borrowers not only need substantial equity, like we've always demanded, but we've enhanced our requirements on good credit and strong reserves as well. We have been able to maintain heightened borrower credit and reserve criteria throughout the last three years, and with the huge void left by the banking industry, coupled with SFG's strong market position, the strategic changes have been performing well. Even with our heightened credit standards, 2010 loan volume increased over 2009 by 52%. We experienced another 15% increase from 2010 through 2011. New loan volume at today's valuations, along with the disposition of non-performing assets, are the ingredients to achieving our immediate objectives. Real progress is being made on both fronts.

Portfolio Balance

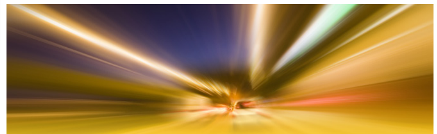
(loans originated in the last three years)

Commercial loans	**43%**
Residential Loans	**57%**
Average loan to value:	**60%**
(at post "crash" valuations).	

Amount of those loans still on the books.

Approximately 30% of the loans originated during the last three years are still on the books today, and as of this writing, 12% of our portfolio is in cash. These statistics demonstrate that our loans are performing, that the strategic changes have taken hold, and that our focus on transitional lending remains relevant and viable to the market. Borrowers are borrowing the money, achieving their objectives and paying us off. Further testament to the effectiveness of our business model is reflected in our ability to maintain liquidity throughout the market collapse. Loans on the books today, dated October 2008 or later, remain below the general economic turbulence and are performing well.

We finished the first two quarters of 2011 in high gear posting over $2 million in profits and shaving 6% off our non-performing asset percentage.



Non-performing asset percentage

(loans originated in the last three years)

Less than 2% of the loans funded since October 2008 have gone past 60 days late. None have produced a loss. Historically our portfolio has averaged between 12-18% in some stage of temporary non-performance, although large equity cushions protected our capital. In addition, the 12-18% of non-performing assets provided a profit center for the fund, paying late fees and default interest. Today, our heightened borrower credit requirements are producing a portfolio of loans that pay on time, hence we are receiving less late fee income. Given the fragile economy, we think it is prudent to lean towards borrowers with stronger pay histories and forgo the potential late fees and ancillary income. Once we meet our target non-performing asset percentage of 16% or less, and when the market indicators warrant, we may decide to relax our credit standards somewhat. However our future credit standards will always be somewhat above our historical norms; SFG will always look toward and maintain a disciplined blend of underwriting factors when approving new loans. We have learned a great deal over the last few years, our fund is stronger, and we are better because of it.

Average borrower credit score: 714

(loans originated in the last three years)

For those of you who do not follow FICO scores, 714 is excellent and unusually high quality for an equity based lender. Equity based lenders generally rely more on equity to protect their position and less on the borrower's credit. We have found that a reasonable balance of borrower quality coupled with our traditional collateral position in marketable real estate best support fund performance in all markets. Today we are confidently obtaining high levels of both credit and equity as we transition toward a portfolio made up of stronger, more experienced sponsors. The economic events of 2008 and 2009 however, have given us reason for permanent upgrades to our borrower credit standards, and those changes will serve us well, long into the future.

New loans are performing on time while protecting our capital and positioning borrowers for substantial profit.

Loan losses 0%

(loans originated in the last three years)

This is where the rubber meets the road. We, of course, recognized the new loans we were capturing not only had strong equity, but strong borrowers as well. However the 0% loan loss statistic really got our attention and remains a confirmation for our actions moving forward. Keep in mind this 0% loan loss the last three years was during the teeth of the worst recession any of us has experienced, an authentic stress test to any real estate loan portfolio.

Conclusion

The actions we began three years ago to protect the fund from declining real estate values is working. We've learned a few things over the last couple years and have made adjustments accordingly. Nonetheless, it was

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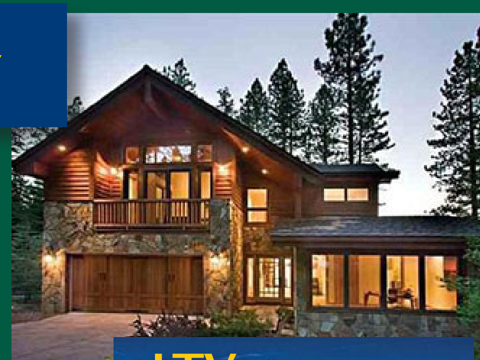
Success Story

New Lake Tahoe Waterfront Residence

$1,700,000

Zephyr Cove, NV

A family trust has owned this waterfront Lake Tahoe property for decades. They decided to partner with a builder and construct a high level spec home. Market conditions naturally dictated a slower sales process; hence the construction loan came due. With a prime waterfront asset, good credit borrowers, low loan to value and a clear exit strategy, this loan was closed inside of 10 days.



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our core underwriting principles and disciplines that allowed us to weather this storm and those critical strengths will remain unchanged. New loans are performing on time while protecting our capital with substantial equity and strong borrowers. However, the sputtering economy continues to resist the speed of our progress and remains our biggest frustration. Loan volume is well below normal levels and the market seems to be missing the sense of urgency necessary to enhance the velocity of our advancement, but progress is being made and we continue to set the pace for others in our industry. We finished the first two quarters of 2011 in high gear posting $2.3 million in profits and shaving 6.4% off our non-performing asset percentage. The summer months of July, August and September were slow. Nevertheless, we keep marching forward insistently and will not rest until we have achieved the objectives before us. We look forward to better economic times ahead and thank you for our business relationship.

> *The sputtering economy continues to resist the speed of our growth.....Nevertheless, we keep marching forward insistently, serving the mortgage community.*

The Team at Seattle Funding Group

Success Story

Luxury Maui Oceanfront Residence

$1,250,000
Business Capital
Kihei, HI

This recent Seattle Funding Group closing is the perfect example of a quick "business use" loan that had the necessary fundamentals and the essential underwriting elements in place for a strong lending opportunity. This mainland owner needed the funds to capitalize his business quickly while negotiating the sale of his company. This luxury beachfront home is located in a very desirable Maui location. The experienced sponsor has excellent financials along with a substantial equity position in the asset. SFG expertly assessed value and closed the transaction in under 10 days, thereby allowing the sponsor to meet his business needs. The securing property is valued in excess of $3,000,000.

Favorite Quotes

Success is liking yourself, liking what you do, and liking how you do it. ~Maya Angelou

I find that the harder I work, the more luck I seem to have." ~Thomas Jefferson

When you do the common things in life in an uncommon way, you will command the attention of the world." ~George Washington Carver

If opportunity doesn't knock, then build a door. ~Milton Berle

Obstacles are those frightful things you see when you take your eyes off your goal." ~Henry Ford

If you have any favorite quotes you'd like to see in this publication, please pass them along to John Odegard. We'd even be happy to mention in our newsletter where they came from. E-mail your favorite quotes to: jodegard@sfgfunds.com.

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