

E-MEMO

TO: INVESTOR/MEMBERS AND FRIENDS
FROM: Jon Bruss
DATE: March 8, 2004
SUBJECT: **Bob Ollech and thoughts on earnings guidance and more on the survival of banks.**

First and foremost, I'd like to introduce you to Bob Ollech who joined Fortress Partners on February 16 as Managing Director—Portfolio Management. Arguably, one of the reasons I'm so pleased that he has joined me is that his presence has allowed me to write this from Bonita Springs, Florida. There are other even better reasons. First of all, Bob is smarter than I am. I have tried to make that a key policy for years in hiring associates. He is certifiably smarter inasmuch as he graduated *magna cum laude* in finance and accounting from the University of Wisconsin—Eau Claire and has recently earned his Chartered Financial Analyst (CFA) certification. He has great banking DNA. His dad is a banker in Wisconsin (I've known his dad for nearly 40 years and had the pleasure of serving as his banker). Bob worked for the Federal Reserve Bank of Chicago, supervising banks in Wisconsin, Illinois and Iowa including Fortress Bancshares, Inc. and Fortress Bank of Westby. That's how I first met Bob. The Fed has always been my regulator of choice. It is a superb training ground. Since his 11-year stint at the Fed, he has served as director of research of Howe Barnes Investments in Chicago, a leading boutique investment firm specializing in small banks and thrifts and was most recently a portfolio manager for a firm in Milwaukee. Bob and I share a zeal for banks and thrifts. I know that he is a great addition to our team.

Last month I wrote about small bank survival. The ink was hardly dry when no less a publication than *Investor's Business Daily* published a front-page-above-the-fold article on February 19 entitled "New Banks Serve Small Business Even As Merger Pace Speeds Up." As you know, I love it when my thinking is validated publicly in such a fashion. According to the article, for the first three quarters of 2003, 94 new banks were formed in the US, 22% more than in 2002. The article went on to point out that 48% of the banks and thrifts in this country have less than \$100 million in assets. That size is quite a bit smaller than what we focus on (\$300 million to \$3 billion in assets) and contrasts with Citigroup's \$1.3 trillion in assets. The author of the article cites several reasons for new bank start-ups:

- Startups typically **focus on small businesses** whose employees and owners typically make frequent trips to the bank and **value face-to-face interaction with bank management.**
- **Integrating two banks** with overlapping services and branches **often means senior and middle management lose their jobs.** "Experienced but disenfranchised bankers often seed startups with their capital and desire to have their own businesses," according to the article. That's a fact. I've done it twice myself. The entrepreneurial spirit lives on!
- **Changed systems or new personnel** prompt some customers to shop for different banks while deals encourage potential investors to put together startups as they contemplate what future buyers may be willing to pay for the bank when they want to sell it.
- **"When a bigger bank buys a smaller one, they anticipate losing 20% of their deposit base,** just because of a lack of services. If it's a \$500 million deposit base, they just lost \$100 million," says Mike Wilson, CEO of Golden State Business Bank in Upton, CA which opened its doors in this Southern California town after four of its directors sold their old bank.
- **Population and income growth also drive new bank chartering** according to the article. It cited three new banks each in Texas, Florida and California in the third quarter of 2003 and four each in Georgia and Minnesota.

I hope we have now demonstrated beyond a doubt that the industry is alive and healthy and that small banks are not going to disappear any time soon. That's a key reason we are in this for the long term. We are investors, not traders, which brings me to the other subject: earnings guidance.

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Some of the banks in which we invest have been talked into providing earnings guidance to the investing public. I really don't know why. Tom Brown, a superb bank stock analyst (www.bankstocks.com) wrote about this subject on February 12. Tom received a response from the Chairman and CEO of Orange County Business Bank, J. P Gough, who, prior to founding the bank in 2000, was director of bank consulting for Deloitte & Touche and previously served as a bank president, loan officer, credit officer and risk manager. He also ran his own bank consulting firm. He sees it this way:

- **Investors**, as opposed to in-and-out speculators, do not want to hear about what you are intending to do, rather, they **want to see what you really do**.
- Some **banks** have **nearly tanked as they responded to the most recent trends touted by analysts**. One idea does **NOT** fit all. Avoiding *trendiness* means that bank management shouldn't be caught on the M & A treadmill either.
- **There are no economies of scale in the expense ratio once a bank hits \$100 million in assets**. Technology is the great equalizer in banking just like the gun became the equalizer of big vs. small men in war. Economizing is realized only by commoditizing the business by removing the "service" factor and replacing it with the volume factor.
- **Shareholders are far better served by consistent growth in earnings, dividends and share value than by selling out**.

We haven't chosen our banks because we think they are targets for buyers but because they have grown earnings, dividends and share value consistently (traits nonetheless admired by acquirers). Our track record, shown below, demonstrates how we have performed for nearly four years focusing on these and other key factors. I hope that as you read this you will come to the conclusion that you should become a part of Foundation Financial Partners. To those of you who are already with us, consider adding to your investment. Your next opportunity is April 1, and we hope you take it. Please give us a call or write us an e-mail to either add to your position or start a new one.

**FEBRUARY 2004
PERFORMANCE HISTORY(1)(2)**

	Inception to date (47 Months) 3/29/00-2/29/04	Three Year Return Annualized 2/28/01-2/29/04	Twelve Months Ending 2/29/04	Two Months Ending 2/29/04
FOUNDATION	+136.27	+27.37%	+33.56%	1.95%
Dow Jones Industrial Average	+4.68%	2.38%	+37.17%	+1.61%
NASDAQ	-54.96%	-1.51%	+52.47%	+1.39%
S & P 500	-18.96%	-1.04%	+38.50%	+3.25%
S & P 600 (Small Cap Index)	+39.88%	+10.57%	+55.67%	+4.85%
NASDAQ Bank Index	+113.22%	+18.56%	+37.26%	+2.90%

- (1) **After** management and other expenses but **before** charges for Performance Allocation
 (2) The performance information has been prepared and presented in compliance with the Performance Presentation Standards of the Association for Investment Management and Research (AIMR-PPS®), the U.S. and Canadian version of the Global Investment Performance Standards (GIPS®). AIMR has not been involved in the preparation or review of this information.

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