

PUBLIC DISCLOSURE

January 20, 2004

COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION

**First State Bank of Hope
09129**

**210 Steele Avenue
P.O. Box 158
Hope, North Dakota 58046-0158**

**Federal Deposit Insurance Corporation
2345 Grand Boulevard, Suite 1200
Kansas City, Missouri 64108**

NOTE: This evaluation is not, nor should it be construed as, an assessment of the financial condition of this institution. The rating assigned to this institution does not represent an analysis, conclusion, or opinion of the federal financial supervisory agency concerning the safety and soundness of this financial institution.

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GENERAL INFORMATION

The Community Reinvestment Act (CRA) requires each federal financial supervisory agency to use its authority when examining financial institutions subject to its supervision, to assess the institution's record of meeting the credit needs of its entire community, including low- and moderate-income neighborhoods, consistent with safe and sound operation of the institution. On conclusion of such examination, the agency must prepare a written evaluation of the institution's record of meeting the credit needs of its community.

*This document is an evaluation of the Community Reinvestment Act performance of **First State Bank of Hope, Hope, North Dakota**, prepared by the **Federal Deposit Insurance Corporation (FDIC)**, the institution's supervisory agency, as of **January 20, 2004**. The agency rates the CRA performance of an institution consistent with the provisions set forth in Appendix A to 12 CFR Part 345.*

INSTITUTION RATING

INSTITUTION'S CRA RATING: This institution is rated "Satisfactory."

The bank's CRA performance depicts a satisfactory record of helping to meet the credit needs of its assessment area, including low- and moderate-income neighborhoods, in a manner consistent with its resources and capabilities. The following supports this rating:

- The bank's average net loan-to-deposit ratio since the last evaluation demonstrates an adequate willingness to lend.
- The bank is helping to meet the credit needs of its assessment area by making a majority of its loans in the assessment area.
- The bank is adequately serving farms of different revenue sizes, including smaller operations.
- Given the bank's location and the demographics of the assessment area, the geographic distribution of borrowers reflects a reasonable dispersion throughout the assessment area.
- The bank has not received any CRA-related complaints since the last evaluation; therefore, this performance criterion was not evaluated.

DESCRIPTION OF INSTITUTION

First State Bank of Hope operates from its only office in Hope, North Dakota. The bank is owned by Hunter Holding Company, a three-bank holding company. At the previous CRA Performance Evaluation, dated February 16, 1999, the FDIC rated the institution “Satisfactory.”

As reported in the September 30, 2003, Report of Condition, the bank had total assets of \$17,151,000, total loans of \$11,662,000, and total deposits of \$15,466,000. Other than the legal lending limit, there are no financial or legal impediments that would restrict the bank’s ability to lend in its assessment area.

As displayed in Table 1, the bank’s lending is dominated by loans to farmers. The largest loan category is agricultural loans, accounting for 87 percent of the total loan portfolio. Operating and real estate loans can be considered as one category since the borrowing base is similar. While the bank offers other products and loan services, no other loan product accounts for even 10 percent of the bank’s portfolio. The bank’s products are consistent with its size, financial capacity, and geographic location. Bank management identified agricultural lending as the primary business focus of the bank.

Table 1—Loan Portfolio Distribution

Loan Type	Dollar Volume	Percent of Total Loans
Real estate secured by farmland (including farm residential and other improvements)	\$2,374	20%
Closed-end loans secured by 1-4 family residential properties, first lien	\$163	1%
Real estate secured by nonfarm nonresidential properties	\$34	<1%
Loans to finance agricultural production and other loans to farmers	\$7,800	67%
Commercial and industrial	\$757	7%
Other consumer loans (includes single payment, installment, and all student loans)	\$356	3%
Other loans	\$178	2%
Total Loans	\$11,662	100%

Source: Report of Condition—September 30, 2003 (dollars in 000s)

DESCRIPTION OF FIRST STATE BANK OF HOPE'S ASSESSMENT AREA

The Community Reinvestment Act of 1977, as amended, requires banks to identify one or more Assessment Areas within which its regulatory agency will evaluate the bank's performance. The area(s) defined by the bank must include its main office, branches, and other deposit-taking remote service facilities, as well as the surrounding geographies in which the bank has originated or purchased a substantial portion of its loans. The assessment area always consists of one of more whole geographies identified as Census Tracts (CTs).

The bank has identified its assessment area as Steele County in eastern North Dakota. What few towns are in the assessment area are quite small. The single largest town is Finley; the 2000 U.S. Census reported its population as approximately 500. Hope's population was reported as approximately 300.

The entire assessment area consists of one CT, identified as CT 9687. Specific information about the CT, including its income classification, is shown in Table 2. CT 9687's income classification is based on the MFI of nonmetropolitan North Dakota.¹

Table 2—Census Tracts in the Assessment Area

CT	County	Median Family Income (MFI)	Percent of Applicable MFI	Income Category	Population
9687	Steele	\$43,914	111%	middle	2,258

Source: 2000 U.S. Census

Management made the following comments:

The assessment area is dependent on agriculture, and the area's major crops are spring wheat, dry edible beans, barley, corn, and sunflowers. While the 1980s experienced drought and the 1990s encountered excess moisture, 2003 resulted in good yields. Some cow-calf operations can be found in the county. The trend is to larger farms, with small farms being purchased by existing farmers.

Hope has no large employers. An electrical contracting company employs about 30 people. A new pasta plant opened in town and has about 20 employees. A small manufacturer employs about 25. The "main street" businesses are struggling as many retail customers are willing to drive to Fargo, North Dakota, (approximately 50 miles southeast of Hope) for shopping. The county is in an empowerment zone, making it eligible for various grants and assistance.

Housing stock is in short supply and old. Few are willing to build new houses since construction costs exceed the resulting value of the home. This housing shortage could

¹ A geography's income level is determined by comparing the 2000 median family income (MFI) for the geography with the applicable 2000 MFI for the nonmetropolitan portion of the state or the MSA in which it is located. According to the U.S. Census, the 2000 MFI of the nonmetropolitan North Dakota was \$39,651. Low-income is defined as less than 50 percent of that MFI, moderate-income is defined as 50 to less than 80 percent, middle-income as 80 to less than 120 percent, and upper-income as 120 percent and over.

limit future economic growth since companies need employees, and employees need housing.

Management believed the area's population has been growing recently; however, the U.S. Census reports a decline of seven percent from 1990 to 2000. The area lags behind North Dakota and the nation in per capita income.² The Bureau of Labor Statistics reports that unemployment in the third quarter of 2003 was lower than the North Dakota and national averages.

Another financial institution has an office in the bank's assessment area. The bank also competes with Farm Credit Services for agricultural loans and with direct financing by implement and vehicle dealers. A member of the community contacted prior to the evaluation stated that the bank aggressively seeks agricultural loans.

Table 3 displays selected demographic data of the assessment area.

Table 3—Demographic Information

	Assessment Area
Population	2,258
Number of families	639
Percent households below poverty	7%
Percent of owner-occupied housing	58%
Percent of renter-occupied housing	17%
Median housing value	\$39,800
Median gross rent	\$271

Source: 2000 U.S. Census

² Bureau of Economic Analysis data for 2001

CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA

Five criteria are used in evaluating a small bank's effectiveness in meeting the financing needs of consumers, agricultural borrowers, and commercial entities within the assessment area. Four of the criteria relate to lending performance, and one addresses responsiveness to CRA-related complaints. The findings for each criterion are evaluated and result in an overall rating for Community Reinvestment Act performance. Furthermore, a bank's compliance with anti-discrimination laws and regulations is considered when evaluating a bank's performance. Comments supporting the conclusions for each criterion are detailed below and on the following pages.

Loan-to-Deposit Ratio

The bank's average net loan-to-deposit ratio since the last evaluation demonstrates an adequate willingness to lend. The average net loan-to-deposit ratio based on 19 quarter-ends since the last evaluation is 68 percent. The average ratio is a slight increase from the average ratio of 64 percent reported in the February 16, 1999, Performance Evaluation.

Four institutions were identified that are similar to the bank with respect to communities served, asset size, and loan products. The average net loan-to-deposit ratios for the last 19 quarter-ends for First State Bank of Hope and the four similarly situated institutions are shown in Table 4.

Table 4—Net Loan-to-Deposit Ratios, Similarly Situated Lenders

Institution (other institutions listed alphabetically)	Location	Average Net Loan-to-Deposit Ratio
<i>First State Bank of Hope</i>	<i>Hope</i>	68%
Farmers and Merchants National Bank	Hatton	63%
Fingal State Bank	Fingal	73%
The First and Farmers Bank	Portland	72%
Security State Bank of Hunter*	Hunter	77%

Source: Reports of Condition March 31, 1999, through September 30, 2003;

** - Affiliate of subject bank*

The bank's ratio is higher than one and lower than three similarly situated lenders, with all the lenders grouped in a narrow, 14 percentage-point range. This is support that the bank is willing to extend credit in an adequate manner.

The bank's relatively low lending limit results in the need to sell portions of larger loans to other financial institutions. These overlines (participations) represent dollars loaned by the bank but not reflected in its loan-to-deposit ratio. The bank also purchases some loans, which increase the ratio, but do not represent loans originated by the bank. As of the evaluation date, the bank had sold over \$4 million of participations and purchased under \$2 million in the previous 12 months.

The average net loan-to-deposit ratio since the last evaluation is reasonable given the bank's size, financial condition, and assessment area credit needs.

Lending in the Assessment Area

The bank is helping to meet the credit needs of its assessment area by making a majority of its loans in the assessment area.

To determine the bank’s performance under this criterion, agricultural lending was reviewed. It is the primary business focus of the bank; loans to farmers make up 87 percent of the loan portfolio. With the assessment area’s economy dependent on agriculture, the bank’s record of lending to farmers is the most indicative of its performance. The other loan categories are neither lending emphases nor substantive products of the bank.

Table 5 displays the loan sample and the universe of loans from which it was chosen. The loan universe represents all agricultural loans extended by the bank during six months preceding the date of the evaluation that remained outstanding on the loan trial balance used in the sample.

Table 5—Loan Sample and Universe

Loan Category	Number of Loans		Dollars in Loans	
	Sample	Universe	Sample	Universe
Agricultural Loans	35	105	\$1,836	\$5,859

Source: FDIC sample from loan trial balance (dollars in 000s)

Table 6 shows that the bank is making the majority of its agricultural loans, by number and dollar, in the assessment area. This is evidence that the bank is helping to meet the agricultural credit needs of its community.

Table 6—Assessment Area Concentration—Agricultural Loans

	Number	Percent	Dollars	Percent
Loans in assessment area	28	80%	\$1,217	66%
Loans outside assessment area	7	20%	\$619	34%
Total sample	35	100%	\$1,836	100%

Source: FDIC sample from loan trial balance (dollars in 000s)

The above information is consistent with an internal bank analysis. Loans are identified by CT on the bank’s records. Using that information, the bank concluded that for 2002, 73 percent by number and 74 percent by dollar of its total loan originations were in the assessment area.

Overall, the analyses demonstrate a good performance given the bank’s size and assessment area credit needs, and it demonstrates the bank’s willingness to reinvest deposits back into the local community through loans.

Borrower Profile

The bank is adequately serving farms of different revenue sizes, including smaller operations.

The loan sample described previously under the heading “Lending in the Assessment Area” was used to evaluate the bank’s performance of lending to farms of different sizes within the assessment area. Therefore, 28 agricultural loans located within the assessment area were further analyzed for this performance factor.

If revenue information was not available from the loan file, gross revenue information was obtained through discussions with bank personnel. Each agricultural borrower was categorized based on this information. Table 7 reflects the results of this analysis and a comparison to demographic data from D&B Corporation.

Table 7—Loan Distribution by Borrower’s Revenue—Agricultural Loans

Gross Revenue	Sample of Farms in Assessment Area		Bank’s Agricultural Lending in Assessment Area			
	Number	Percent	Number	Percent	Dollars	Percent
less than \$50	2	5%	3	11%	\$12	1%
\$50-\$99	17	46%	2	7%	\$9	1%
\$100-\$249	15	41%	3	11%	\$37	3%
\$250-\$499	3	8%	11	39%	\$344	28%
\$500-\$999	0	0%	3	11%	\$110	9%
\$1,000 and up	0	0%	6	21%	\$705	58%
Totals	37	100%	28	100%	\$1,217	100%

Source: D&B Corporation and FDIC sample from loan trial balance (dollars in 000s)

Table 7 shows the bank’s performance in lending to farms of various revenue categories. Comparing the 2003 D&B Corporation farm data to the bank’s percentage by number of loans is considered more meaningful than comparing it to dollars lent, as the 2003 D&B Corporation farm data is based on the number of farms in each revenue category.

The bank’s performance, as measured in Table 7, shows that the bank is lending to farms in all revenue categories. The D&B Corporation reports farmers with revenues of \$50,000 to \$249,000 represent 87 percent of all farmers in the assessment area. Only 18 percent of the bank’s lending was to farmers in those revenue ranges. This apparent weakness requires further discussion.

Bank management state that they lend to all farmers they possibly can and expressed skepticism regarding the D&B Corporation data. They stated that a self-sufficient farm requires revenue of about \$600,000, which means that farms below that must have owners with off-farm wages for the operation to be viable. This means that many of the smaller farms in the D&B Corporation data are hobby farms and do not require bank financing. They pointed out that the bank provides a variety of loan programs for applicants who do not qualify for traditional bank financing, including loans through the Farm Service Agency and the United States Department of Agriculture.

Considering these comments, the bank is adequately serving farms of different revenue sizes, including smaller operations.

Geographic Distribution of Loans

Given the bank’s location and the demographics of the assessment area, the geographic distribution of borrowers reflects a reasonable dispersion throughout the assessment area.

The assessment area consists of only one CT, so it is problematic to analyze the bank’s lending by geography. Included in the loan sample described previously under the heading “Lending in the Assessment Area” are loans to farmers in Hope, Luverne, and Finley. Those are three of the

four incorporated towns in the assessment area. The fourth town, Sharon, only has a population of approximately 100³ and is in the far northwest corner of the assessment area. Between Sharon and Hope lies Finley, which is the home office of a competing bank. Therefore, it is reasonable that none of the sampled loans were to farmers in the Sharon area. This is additional evidence that the bank is not excluding lending anywhere in its assessment area.

Response to CRA-Related Complaints

The bank has not received any CRA-related complaints since the last evaluation; therefore, this performance criterion was not evaluated.

Compliance with Anti-discrimination Laws and Regulations

No violations of the substantive provisions of the anti-discriminatory laws and regulations were identified during the evaluation.

³ 2000 U.S. Census