



Comptroller of the Currency
Administrator of National Banks
Washington, DC 20219

SMALL BANK

PUBLIC DISCLOSURE

September 7, 2004

COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION

**First National Bank
Charter Number 7772**

**1018 Hobart Street
Hawley, MN 56549**

**Comptroller of the Currency
North Dakota & NW Minnesota Field Office
3211 Fiechtner Drive SW
Fargo, ND 58103**

NOTE: This document is an evaluation of this 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. 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.

Table of Contents

Institution's Rating	1
Description of Institution	1
Description of Assessment Area	2
Loan Sampling	3
Conclusions about Performance Criteria.....	4
Loan-to-Deposit Ratio.....	4
Lending in Assessment Area.....	5
Lending to Borrowers of Different Incomes and to Farms of Different Sizes.....	6
Geographic Distribution of Loans.....	7
Responses to Complaints.....	7
Fair Lending.....	7

INSTITUTION'S CRA RATING

This institution is rated Satisfactory.

The satisfactory rating is supported by the following factors:

- The bank's loan-to-deposit ratio meets the standard for satisfactory performance.
- The bank's record of lending to farm, business, consumer and real estate borrowers in the Assessment Area meets the standard for satisfactory performance.
- The bank's record of lending to farm, business, consumer and real estate borrowers of different sizes and income levels meets the standard for satisfactory performance.

DESCRIPTION OF INSTITUTION

First National Bank (FNB) is a \$58 million institution located in Hawley, MN. The community is located in Clay County in northwestern Minnesota. FNB has its main office in Hawley, MN and a branch office located in Dilworth, MN. The bank has 3 ATMs, one located at each branch office and one at the Cormorant Pub. The bank is wholly owned by the bank holding company, First Hawley Bancshares, Inc., located in Hawley, MN.

FNB is a full service bank offering traditional loan and deposit products and services. During the assessment period, the bank's primary lending focus was in the area of residential real estate loans and additional activity was focused in the areas of farm, consumer, and business loans. As of June 30, 2004, the composition of the bank's loan portfolio was as follows:

Loan Portfolio Composition	\$ (000)	%
Residential Real Estate Loans	15,623	31.2%
Farm Loans (including real estate)	13,947	27.8%
Business Loans (including real estate)	13,619	27.2%
Consumer Loans	6,778	13.5%
Other Loans	182	.3%
Total	50,149	100%

There are no legal or financial impediments that restrict the bank's ability to meet the credit needs of the community. FNB was rated "Satisfactory" at the last CRA examination dated January 25, 1999.

DESCRIPTION OF FIRST NATIONAL BANK OF HAWLEY'S ASSESSMENT AREA

FNB's assessment area (AA) includes five contiguous census tracts (CTs), all located in Clay County in northwestern Minnesota. All of the CTs in the AA are middle-income. The AA is part of the Fargo/Moorhead Metropolitan Statistical Area (MSA). Cities in the AA include, but are not limited to Hawley, Dilworth, Glyndon, Barnesville, Sabin, and Ulen. Primary competition includes full service, similarly sized banks within its AA. Secondary competition comes from regional and mid-size banks located in the Fargo/Moorhead and Detroit Lakes areas, which are adjacent to the bank's AA. According to the 2000 census, the population of the AA was 19,018, which is a decrease of approximately 408 persons since the 1990 census.

Local employers in the area include farm machinery and equipment manufacturers, education and health services and governmental jobs. Information from the Bureau of Labor Statistics lists the 2003 unemployment rate for Clay County at 3.1% with 6.5% of the total population living below the poverty level. The average unemployment rate in 2003 for Minnesota was 5.0% and 6.0% nationwide.

During our evaluation, we contacted a local city official. Credit needs in the community continue to focus on residential real estate. Small business and farm loans are still a primary need in this bank's AA.

The demographics of the AA are listed in the table on the next page. The information is based on 2000 census data unless otherwise noted.

Demographic and Economic Characteristics of the AA	
<i>Population</i>	
Number of Families	5,194
Number of Households	6,944
Number of Low-Income Families	933
% of Low-Income Families	18%
Number of Moderate-Income Families	1,028
% of Moderate-Income Families	19.8%
Number of Middle-Income Families	1,475
% of Middle-Income Families	28.4%
Number of Upper-Income Families	1,758
% of Upper-Income Families	33.8%
<i>Geographies</i>	
Number of Census Tracts/BNA	5
% Low-Income Census Tracts/BNA	0%
% Moderate-Income Census Tracts/BNA	0%
% Middle-Income Census Tracts/BNA	100%
% Upper-Income Census Tracts/BNA	0%
<i>Median Family Income (MFI)</i>	
2000 MFI for AA	\$49,309
2003 HUD-Adjusted MFI	\$60,100
<i>Economic Indicators</i>	
2003 Unemployment Rate- Clay County	3.1%
% of Households Below Poverty Level	6.5%

LOAN SAMPLING

The bank's primary loan types were determined by reviewing all loans originated from January 25, 1999 to September 1, 2004. In determining primary loan products, consideration is given to both the number and dollar volume of loans originated and purchased during the allotted time frame.

For the purposes of this evaluation, the primary loan types are residential real estate loans, farm loans, business loans, and consumer loans. Residential real estate loans make up 13% of the number and 31% of the dollar volume of loans originated. Consumer loans make up 50% of the number and 14% of the dollar volume of loans originated. Business loans make up 17% of the number and 27% of the dollar volume of loans originated, while farm loans make up 20% of the number and 28 % of the dollar volume of loans originated.

The following table depicts a breakdown of originations in our evaluation period.

Loan Products	#	%	\$ (000)	%
Residential Real Estate Loans	205	13%	13,406	31%
Consumer Loans	795	50%	6,054	14%
Farm Loans (including real estate)	313	20%	12,108	28%
Business Loans (including real estate)	267	17%	11,677	27%
Total	1,580	100%	43,245	100%

Source: Loan Sample

To conduct our analysis, we performed statistically valid sampling techniques in selecting a sample of twenty residential real estate loans, twenty farm loans, twenty consumer loans, and twenty business loans. After initial sampling to determine the bank's lending within the AA, additional files were selected so that all loans used in the borrower distribution analysis were made within the AA.

CONCLUSIONS ABOUT PERFORMANCE CRITERIA

Loan-to-Deposit Ratio

FNB's loan-to-deposit ratio (LTD) meets the standard for satisfactory performance given the bank's size, financial condition, and lending opportunities within its AA. The quarterly LTD ratio averaged 86.71% since the last CRA examination.

When compared to five similarly situated banks' loan-to-deposit ratios in the AA, FNB ranked second out of six banks. These banks have asset sizes ranging from \$35 million to \$116 million. The average LTD ratio of all six banks for the evaluation period is 80%.

Loan-to-deposit Institution	Assets as of 6/30/04 (\$000s)	Average LTD Ratio (%)
First State Bank of North Dakota	75,498	90.73
First National Bank, Hawley, MN	61,030	86.71
Northwestern Bank, National Association	115,539	83.08
Union State Bank of Fargo	34,564	79.65
Security State Bank of Hunter	34,788	74.66
State Bank of Hawley	61,295	65.11

**Source: Consolidated Reports of Condition for the evaluation period.*

Lending in Assessment Area

FNB meets the standards for satisfactory performance for lending within the AA. A majority of the loans were originated in the bank's AA. The following table illustrates lending activity within the AA during the evaluation period.

Table 1 - Lending in FNB's Assessment Area										
Loan Type	Number of Loans					Dollars of Loans				
	Inside		Outside		Total	Inside		Outside		Total
	#	%	#	%		\$ (000)	%	\$ (000)	%	
Residential RE Sample	18	90%	2	10%	20	1,524	90%	178	10	1,702
Farm Loan Sample (including RE)	16	80%	4	20%	20	1,264	82%	271	18%	1,535
Consumer Loan Sample	19	95%	1	5%	20	287	98%	5	2%	292
Business Loan Sample (including RE)	17	85%	3	15%	20	2,460	97%	87	3	2,547
Totals	70	87.50%	10	12.50%	80	5,535	91%	541	9%	6,076

Source: Loan Sample

Lending to Borrowers of Different Incomes and to Businesses of Different Sizes

Overall, lending to borrowers of different incomes and businesses of different sizes meets the standard for satisfactory performance.

Residential Real Estate Loans

The borrower distribution of residential real estate loans to low- and moderate-income households approaches meeting the demographics of the AA. When giving consideration to the bank's performance context, the bank performs adequately with regard to low-income borrowers. Over 7% of households in the AA are below the poverty level, leaving only approximately 11% of low-income borrowers available for residential real estate loan qualification.

Borrower Distribution of Residential Real Estate Loans in FNB's Assessment Area								
Borrower Income Level	Low		Moderate		Middle		Upper	
	% of AA Families	% of Number of Loans	% of AA Families	% of Number of Loans	% of AA Families	% of Number of Loans	% of AA Families	% of Number of Loans
Residential RE Loans	18.0%	5%	19.8%	10%	28.4%	40%	33.8%	45%

Source: Loan Sample; 2000 U.S. Census data

Farm Loans

Lending to farms of different sizes meets the standards of satisfactory performance. Lending to farms with revenues under \$1 million approaches the standards of the demographics of the AA. The following table illustrates FNB's lending to farms.

Borrower Distribution of Loans to Farms in FNB's Assessment Area				
Farm Revenues (or Sales)	≤\$1,000,000	>\$1,000,000	Unavailable/ Unknown	Total
% of AA Farms	95.08%	3.69%	1.23%	100%
% of Bank Loans in AA by #	90%	5%	5%	100%
% of Bank Loans in AA by \$	97%	2%	1%	100%

Source: Loan sample; 2000 U.S. Census data

Consumer Loans

The borrower distribution of consumer loans to low- and moderate-income households exceeds the demographics of the AA.

Borrower Distribution of Consumer Loans in FNB's Assessment Area								
Borrower Income Level	Low		Moderate		Middle		Upper	
	% of AA Households	% of Number of Loans	% of AA Households	% of Number of Loans	% of AA Households	% of Number of Loans	% of AA Households	% of Number of Loans
Consumer Loans	19.0%	35%*	14.8%	35%*	20.7%	15%*	45.5%	10%*

Source: Loan Sample; 2000 U.S. Census data

*5% of loans did not contain borrower income information

Business Loans

Lending to businesses with revenues under \$1 million exceeds the standards for satisfactory performance. The distribution of number of loans and dollar volume of loans exceeds the standards of satisfactory performance.

Borrower Distribution of Loans to Businesses in Assessment Area				
Business Revenues (or Sales)	≤\$1,000,000	>\$1,000,000	Unavailable/ Unknown	Total
% of AA Businesses	67.71%	4.24%	28.05%	100%
% of Bank Loans in AA by #	80%	5%	15%	100%
% of Bank Loans in AA by \$	97%	3%	0%	100%

Source: Loan sample; 2000 U.S. Census data

Geographic Distribution of Loans

Geographic distribution of loans was not completed since the bank's AA does not contain any low- or moderate-income CTs, therefore an analysis of geographic distribution is not meaningful.

Responses to Complaints

FNB's response to complaints meets the standard for satisfactory performance. During the evaluation period, FNB received two complaints. One complaint questioned the legality of an advertisement made by FNB for consumer loans with an APR of 4.9% for 6 months. The second complaint disputed the FNB's decision to deny the complainant a loan due to unpaid tax liens. In both cases it was found that the bank was technically correct, the consumers were informed of these findings, and the cases were closed.

Fair Lending or Other Illegal Credit Practices Review

An analysis of public comments and consumer complaint information was performed according to the OCC's risk based fair lending approach. During our examination, we found no evidence of illegal discrimination or other illegal credit practices.