



SMALL BANK

Comptroller of the Currency
Administrator of National Banks

Public Disclosure

March 11, 2002

Community Reinvestment Act Performance Evaluation

**THE FIRST NATIONAL BANK IN WADENA
Charter Number: 12507**

**25 S.W. Bryant Street, P.O. Box 111
Wadena, Minnesota 56482**

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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.

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Institution's CRA Rating

This institution is rated **Outstanding**.

The First National Bank in Wadena's rating is based on the following factors:

- ◆ The bank's performance in lending to borrowers of different incomes and businesses and farmers of different sizes is excellent.
- ◆ The geographic distribution of the loans sampled exceeds standards for satisfactory performance. A majority of the bank's loans are made to borrowers in moderate-income tracts.
- ◆ The bank's lending within its assessment area exceeds the standards for satisfactory performance. A substantial majority of the bank's loan originations are made in their assessment area.

Description of Institution

The First National Bank in Wadena (FNB) is located in Wadena County in Wadena, Minnesota. FNB's assets total \$43 million as of December 31, 2001. The bank does not operate any branches and has one non-deposit taking ATM. The First National Agency of Wadena, Inc., a one-bank holding company, owns 100% of the bank. There have been no acquisitions or mergers since the previous CRA evaluation. The bank's holding company converted to a Subchapter S Corporation during the first quarter of 1999.

The bank's loan portfolio is diverse. As of December 31, 2001, the composition of the portfolio is as follows:

| Loan Portfolio Composition | \$ (000) | % |
|---|-----------------|-------------|
| Residential Real Estate | 9,369 | 42% |
| Agricultural Loans (including Real Estate) | 5,875 | 26% |
| Commercial (including Real Estate) | 4,292 | 20% |
| Consumer Loans | 1,991 | 9% |
| Construction | 488 | 2% |
| Other Loans | 273 | 1% |
| Obligations of State & Political Subdivisions | 39 | 0% |
| Total | 22,327 | 100% |

The bank is conservative in its business strategy and lending philosophy. FNB offers traditional banking products and focuses its lending on consumer, agriculture, commercial, and residential real estate loans. Total loans represent 50% of total bank assets. Tier One Leverage Capital for the bank is 7.75% of average assets or nearly \$3.5 million.

There are no legal impediments that would restrict the bank's ability to meet the credit needs of the community.

FNB was rated "Satisfactory" at the last CRA evaluation dated February 11, 1997.

Description of First National Bank in Wadena's Assessment Area

FNB's assessment area (AA) includes six block-numbering areas (BNAs) in parts of Wadena, Todd, and Otter Tail counties. Three BNAs are designated as moderate-income tracts and three BNAs are designated as middle-income tracts. There are no low- or upper-income tracts in the bank's AA. The median family income updated by HUD for the year 2001 for the state of Minnesota is \$47,100.

The AA includes only whole BNAs that are contiguous. The AA meets the requirements of the regulation. The AA does not arbitrarily exclude low- or moderate-income geographies. Cities included in the AA are Wadena, Verndale, Hewitt, Sebeka, New York Mills, and Deer Creek.

The bank's AA is dependent on agriculture, primarily cash crops and dairy. The agricultural economy experienced unstable economic conditions over the past several years. Government subsidies, insurance coverage, and off-farm income assisted local farmers. Employment opportunities outside of farming include the area school district, a patio furniture manufacturing plant, and the local hospital and clinic. Based on 1990 census data, there were 1,912 farm and non-farm businesses in the AA. Of these, 90% are considered small businesses with annual revenue of less than \$1 million.

The bank's major competitors include financial institutions located in Wadena, Sebeka, Deer Creek, and New York Mills. These banks range in size from \$16 to \$81 million in assets. Wadena State Bank of Wadena is the bank's primary competition.

During our evaluation, we contacted a housing and development organization and an agricultural organization to discuss the credit needs in the community. Primary credit needs identified by these contacts included revitalization of existing housing, affordable elderly housing, as well as a continued demand for agricultural credit.

The demographics of the AA are illustrated in the table below. The information is based on the 1990 census data unless otherwise noted. This is the most recent information available during our evaluation.

| DEMOGRAPHIC AND ECONOMIC CHARACTERISTICS OF AA | |
|---|----------|
| <i>Population</i> | |
| Number of Families | 6,527 |
| Number of Households | 9,078 |
| Number of Low-Income Families | 1,903 |
| % of Low-Income Families | 29.16% |
| Number of Moderate-Income Families | 1,310 |
| % of Moderate-Income Families | 20.07% |
| Number of Middle-Income Families | 1,539 |
| % of Middle-Income Families | 23.58% |
| Number of Upper-Income Families | 1,775 |
| % of Upper-Income Families | 27.19% |
| % Minority Population | 0.80% |
| <i>Geographies</i> | |
| Number of Census Tracts/BNA | 6 |
| % Low-Income Census Tracts/BNA | None |
| % Moderate-Income Census Tracts/BNA | 3 |
| % Middle-Income Census Tracts/BNA | 3 |
| % Upper-Income Census Tracts/BNA | None |
| <i>Median Family Income (MFI)</i> | |
| 1990 MFI for AA | \$28,933 |
| 2001 HUD-Adjusted MFI | \$47,100 |
| <i>Economic Indicators</i> | |
| Unemployment Rate | 2.43% |
| 2001 Median Housing Value | \$36,982 |
| % of Households Below Poverty Level | 21.83% |

Conclusions about Performance Criteria

The bank's CRA performance is based on the assessment of five criteria. We selected a sample from the bank's primary loan products originated since January 2000 to assess the bank's performance. Our assessment did not include loans originated prior to January 2000 due to limitations with loan processing software. The primary loan products for FNB are consumer automobile-secured, consumer unsecured, agricultural, commercial, and residential real estate loans. We also conducted interviews with people in the community and reviewed the bank's public CRA file as part of our evaluation process.

FNB's strength is its willingness to lend in its assessment area and lend to low- and moderate-income borrowers.

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

The bank's lending to borrowers of different incomes and businesses of different sizes is strong and exceeds standards for satisfactory performance. FNB's primary loan products were determined by examining the percentage of loans originated by dollar amount and by number of originations. Consumer automobile-secured and unsecured consumer loans were chosen at FNB's request because of the high number of loans originated for these products. Agriculture, commercial, and residential real estate were chosen based on the dollar volume of loans originated.

Consumer Automobile-Secured Loans

The bank's lending practices for consumer automobile-secured loans compare favorably to the demographic data. The data for the bank's AA reflects that 33% of households are low-income and 17% are moderate-income. The bank's lending practices for consumer automobile secured loans indicate that 67% by number and 53% by dollar are made to low-income borrowers and 30% by number and 35% by dollar are extended to moderate-income borrowers. The table below summarizes income levels of the 30 consumer automobile-secured loans we sampled that were originated since January 1, 2000 in the bank's AA.

| CONSUMER AUTOMOBILE-SECURED LOANS | | | | |
|--|--|--|---|--|
| Borrower Income Level | LOW <50% of median family income | MODERATE At least 50% and <80% of median family income | MIDDLE At least 80% and <120% of median family income | UPPER >120% of median family income |
| % of Households | 33% | 17% | 19% | 31% |
| Number of Loans | 20 | 9 | 1 | 0 |
| % by Number | 67% | 30% | 3% | 0% |
| Dollar of Loans | \$112,000 | \$74,000 | \$27,000 | \$0 |
| % by Dollar | 53% | 35% | 12% | 0% |

Unsecured Consumer Loans

The bank’s lending practices for unsecured consumer loans exceeds the demographic data for the bank’s AA. The data illustrates that 33% of the bank’s AA is low-income and 17% is moderate-income. The lending practices of the bank show that 63% by number and 31% by dollar of miscellaneous purpose consumer loans are extended to low-income individuals and 34% by number and 58% by dollar to moderate-income individuals. The table below summarizes income levels of the 30 unsecured consumer loans we sampled that were originated since January 1, 2000 in the bank’s AA.

| UNSECURED CONSUMER LOANS | | | | |
|---------------------------------|--|--|---|--|
| Borrower Income Level | LOW <50% of median family income | MODERATE At least 50% and <80% of median family income | MIDDLE At least 80% and <120% of median family income | UPPER >120% of median family income |
| % of Households | 33% | 17% | 19% | 31% |
| Number of Loans | 19 | 10 | 1 | 0 |
| Percentage Number | 63% | 34% | 3% | 0% |
| Dollar Amount of Loans | \$23,000 | \$43,000 | \$8,000 | \$0 |
| Percentage Number | 31% | 58% | 11% | 0% |

Agriculture Loans

The bank’s lending practices for small farm loans are consistent with the demographic data. The data reflects that 97% of the farms in the AA have revenues of less than \$1 million. Of the loans sampled, 100% had revenues less than \$1 million. The table below summarizes income levels of the 30 agriculture loans we sampled that were originated since January 1, 2000 in the bank’s AA.

| BORROWER DISTRIBUTION OF LOANS TO SMALL FARMS | | |
|--|---------------------|---------------------|
| Farm Revenues | ≤\$1,000,000 | ≥\$1,000,000 |
| % of Farms in AA | 97% | 3% |
| % of Bank Loans in AA by # | 100% | 0% |
| % of Bank Loans in AA by \$ | 100% | 0% |

Commercial Loans

The bank’s lending practices for commercial loans are consistent with the demographic data. The data reflects that 88% of businesses have revenues of less than a \$1 million. Of the loans sampled, 95% by dollar amount had revenues well below this level. The table below summarizes income levels of the 30 commercial loans we sampled that were originated since January 1, 2000 in the bank’s AA.

| BORROWER DISTRIBUTION OF LOANS TO SMALL BUSINESSES | | |
|---|---------------------|---------------------|
| Business Revenue | ≤\$1,000,000 | ≥\$1,000,000 |
| % of Businesses in AA | 88% | 8% |
| % of Bank Loans in AA by # | 87% | 13% |
| % of Bank Loans in AA by \$ | 95% | 5% |

Residential Real Estate Loans

The bank’s lending practices for residential real estate loans are consistent with the demographic data information. The data indicates that 29% of the families in the AA were considered low-income and 20% moderate-income. Our residential real estate loan sample reveals that 20% of loan originations by number are extended to low-income families and 23% by number are extended to moderate-income families. The table below summarizes income levels of the 30 residential real estate loans we sampled that were originated since January 1, 2000 in the bank’s AA.

| RESIDENTIAL REAL ESTATE LOANS | | | | |
|--------------------------------------|---|---|--|--|
| Borrower Income Level | LOW <50% of median family income* | MODERATE At least 50% and <80% of median family income* | MIDDLE At least 80% and <120% of median family income* | UPPER >120% of median family income* |
| % of Families | 29% | 20% | 24% | 27% |
| Number of Loans | 6 | 7 | 10 | 7 |
| Percentage of Number | 20% | 23% | 34% | 23% |
| Dollar Amount of Loans | \$100,000 | \$214,000 | \$541,000 | \$562,000 |
| Percentage of Dollar | 7% | 15% | 38% | 40% |

* Median family income for 2001 is \$47,100.

Residential real estate lending to low-income families appears low. However, the demographic information regarding FNB’s AA indicates that 22% of the population lives below the poverty level. The low-income borrowers may not qualify for a residential real estate loan.

Geographic Distribution of Loans

The distribution of the bank's loans exceeds the standards for satisfactory performance. The bank's AA includes 3 moderate-income tracts and 3 middle-income tracts. Upon review of FNB's primary loan products, we determined the bank lends in all income tracts in their AA. The table below illustrates the demographic data for the AA and the findings from our review.

| Loan Type | MODERATE -INCOME TRACTS | MIDDLE- INCOME TRACTS |
|------------------------------------|--|--------------------------------------|
| Consumer Automobile Secured | | |
| % of Households | 45% | 55% |
| FNB Performance by # | 50% | 50% |
| FNB Performance by \$ | 58% | 42% |
| Unsecured Consumer | | |
| % of Households | 45% | 55% |
| FNB Performance by # | 47% | 53% |
| FNB Performance by \$ | 32% | 68% |
| Agriculture | | |
| % of Farms | 54% | 46% |
| FNB Performance by # | 100% | 0% |
| FNB Performance by \$ | 100% | 0% |
| Commercial | | |
| % of Businesses | 32% | 68% |
| FNB Performance by # | 80% | 20% |
| FNB Performance by \$ | 94% | 6% |
| Residential Real Estate | | |
| % of Owner Occupied | 48% | 52% |
| FNB Performance by # | 63% | 37% |
| FNB Performance by \$ | 58% | 42% |

Lending in Assessment Area

The bank exceeds the standards for satisfactory performance within its assessment area. FNB's lending patterns indicate a substantial majority of loans are originated within their AA. Internal bank reports calculate the lending inside and outside the AA using all loans originated. The reports indicate that 89% of the loans originated in 2001 were extended to borrowers within the AA. We verified the reports by sampling 30 loans totaling \$395 thousand across the bank's primary product types originated since January 1, 2000. Ninety-six percent of the number of loans sampled and 90% of the volume of loans sampled were originated within the bank's AA.

Loan-to-Deposit Ratio

FNB's loan-to-deposit ratio meets the standards for satisfactory performance given the size and financial condition of the bank, assessment area needs, and local economic conditions. Since the last CRA evaluation, the bank's average quarterly loan-to-deposit ratio is 52%. The bank's loan-to-deposit ratio as of December 31, 2001 is 59%. FNB's trend in lending is increasing. The loan demand in the AA is not high as evidenced by the other bank's loan-to-deposit ratios. Twenty-two percent of households in the AA are below the poverty level, which could lead to difficulty in originating loans.

When compared to five other similarly situated banks in the AA FNB is ranked fifth out of the six banks. All of these financial institutions are of a similar size, located in close proximity to one another, and offer similar loan products. The average quarterly loan-to-deposit ratios range from 39% to 66%. The following table depicts the comparison of these banks.

| Institution | Assets 12/31/01 | Average Quarterly LTD Ratio |
|--|----------------------------|--|
| Farmers & Merchants State Bank of New York Mills | \$49 Million | 66.05% |
| Security State Bank of Sebeka | \$23 Million | 65.78% |
| First National Bank of Henning | \$58 Million | 64.87% |
| Wadena State Bank of Wadena | \$81 Million | 61.10% |
| First National Bank in Wadena | \$44 Million | 52.17% |
| Security State Bank of Deer Creek | \$16 Million | 39.41% |

Other Lending and Investment Activity

We reviewed the bank's qualified investments, community development loans, and housing loans originated by FNB and sold on the secondary market. These activities enhance FNB's lending performance. Examples of FNB's activities during the evaluation period include:

- ◆ FNB purchased two qualified investments for a total of \$170 thousand in Wadena Housing and Redevelopment Authority
- ◆ FNB purchased one qualified investment for \$50 thousand in the Wadena-Deer-Creek School District.
- ◆ FNB originated a \$29 thousand loan for the development of a community youth center.
- ◆ FNB originated and sold 43 housing loans on the secondary market for a total of \$456 thousand.

Responses to Complaints

FNB has not received any complaints about its performance in helping to meet the credit needs of the community since the prior CRA evaluation.

Fair Lending Review

An analysis of two years public comments and consumer complaint information since 1997 was performed according to the OCC's risk based fair lending approach. Based on its analysis of the information, the OCC decided that a comprehensive fair lending examination need not be conducted in connection with the CRA evaluation this year. The latest comprehensive fair lending exam was performed in 1997.