

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 operations of the institution. Upon 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 CRA performance of **Farmers State Bank, Breckenridge, Michigan** prepared by the **Federal Reserve Bank of Chicago**, the institution's supervisory agency, as of **April 29, 1996**. The agency rates the CRA performance of an institution consistent with the provisions set forth in Appendix A to 12 CFR Part 228.

INSTITUTION-S RATING: This institution is rated Satisfactory.

The bank promotes economic revitalization and growth consistent with its size, financial capacity, location, and current economic conditions. The bank originated the majority of its commercial/agricultural, consumer installment, and real estate mortgage loans within its assessment area. The geographic distribution of loans demonstrates a reasonable penetration of all segments of the bank's community. The distribution of borrowers reflects a reasonable penetration among individuals of different income levels, and businesses and farms of different sizes. The loan-to-deposit ratio is reasonable, given the bank's size, financial condition, and assessment area credit needs. The bank's assessment area meets the definition and purpose of the CRA, and does not arbitrarily exclude any low- or moderate-income areas or residents that it would reasonably be expected to serve.

The following table indicates the performance level of **Farmers State Bank, Breckenridge, Michigan** with respect to each of the five performance criteria.

SMALL INSTITUTION ASSESSMENT CRITERIA	FARMERS STATE BANK PERFORMANCE LEVELS		
	Exceeds Standards for Satisfactory Performance	Meets Standards for Satisfactory Performance	Does Not Meet Standards for Satisfactory Performance
Loan-to-Deposit Ratio		X	
Lending in Assessment Area		X	
Lending to Borrowers of Different Incomes and to Businesses of Different Sizes		X	
Geographic Distribution of Loans		X	
Response to Complaints	No complaints were received since the previous consumer compliance examination.		

DESCRIPTION OF INSTITUTION

Farmers State Bank, with assets of \$89.3 million as of March 31, 1996, is a subsidiary of FSB Bankcorp, Inc., a one-bank holding company. This rural bank has three banking offices located in Breckenridge (main office), Ithaca and Hemlock (both branch locations). From these locations, the bank offers a variety of deposit services, including on-line automated teller machines (ATMs).

The bank offers residential, agricultural, commercial, consumer, and government guaranteed loans. Loans, trust and data processing services are centralized at the main office, while credit card services are provided through an outside vendor. The bank's primary business focus is to provide retail banking services that will assist local residents, farmers, and businesses in meeting their credit and deposit needs. The bank's credit and deposit products appear to be consistent with the community's credit needs.

Competition for credit and deposit products within the delineated community is provided by the following Michigan financial institutions: Bank of Alma, with branches in Ithaca and St. Louis; Commercial Bank, with branches in Ithaca, Middleton and St. Louis; Chemical Bank and Trust Company, with branches in Breckenridge and St. Louis; NBD Bank and Second National Bank of Saginaw, each with a branch in Hemlock.

DESCRIPTION OF THE BANK-S ASSESSMENT AREA

The bank has defined its assessment area as the entirety of 20 townships, which extend into three counties (Gratiot, Midland, Saginaw) and consist of seven census tracts and five block numbering areas (BNAs). The seven census tracts in the bank's assessment area are located in Midland and Saginaw Counties, which are within the Saginaw-Bay City-Midland Metropolitan Statistical Area (MSA). The assessment area approximates a rectangularly shaped area located 45 miles north of Lansing, Michigan. According to 1990 U.S. census data, the assessment area has a population of 44,435. Minorities comprise 3.4% of the total population, while the largest segment of the minority population is individuals of Hispanic decent (2.2%). The assessment area contains no minority or low-income census tracts or BNAs; however, there are two moderate-income census tracts, one in each of the counties of Midland and Saginaw, within the bank's assessment area. The median family income in the assessment area is \$32,101. The breakdown of families within the assessment area, by income level, is as follows: low-income - 19.0%; moderate-income - 18.3%; middle-income - 23.0%; upper-income - 39.7%.

Homes in the assessment area have a median value of \$43,378 and a median age of 28 years. This compares to the statewide median home value of \$60,062 and median age of 26 years. The housing stock in the assessment area is 79.5% owner-occupied single-family homes.

Some of the primary employers within the community include: Aircraft Precision Products Incorporated; Precision Plastic and Die Company; Gratiot Community Hospital; Total Petroleum, Incorporated; B & W Coop (local farmers cooperative); area schools; General Telephone Company and United Technologies. The State of Michigan's unemployment rate is 4.5%.

according to the April 1996 Michigan Employment Security Commission Area Labor Statistics. This compares to an unemployment rate of 4.4%, 6.0%, and 5.4%, for Midland, Gratiot, and Saginaw Counties, respectively, for the same period.

The assessment area contains the City of Ithaca, and the Villages of Breckenridge, Hemlock, Merrill, North Star and Wheeler. This area has traditionally been a farming community; however, growth in the surrounding communities has created a population mix of approximately 50% commuters. This has increased the demand for real estate lending which is evidenced by the bank's 14.5% increase in real estate loans in the past year (according to the March 31, 1995 Uniform Bank Performance Report). According to three community representatives, contacted to assist in the review of the bank's CRA performance, the demand for housing is strong while the available vacant land is limited. New subdivisions are being developed as soon as land becomes available. Additionally, the community contacts stated, business growth in the community has remained stable. New businesses have moved into the community at a level slightly greater than businesses have moved out or closed. The community contacts indicated that housing for senior citizens is a more specific need in the community. One community contact stated approximately 65% of the bank's local area residents are retirees.

CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA:

Loan-to-Deposit Ratio

A review of the bank's March 31, 1996 Consolidated Report of Condition revealed a loan-to-deposit ratio of 68.93%. An analysis of the bank's Consolidated Reports of Condition for the five quarters since the previous examination revealed an average loan-to-deposit ratio of 71.80%. According to the Uniform Bank Performance Report (UBPR), the bank's ratio compares favorably with the bank's peer group. As of March 31, 1996, the bank's peer loan-to-deposit ratio was 60.57%. The bank's overall lending performance exceeds that of its peers by approximately 14%, as of March 31, 1996. The most significant variance between the bank and the peer group's performance was noted in total loans. Approximately 64% of the bank's assets were loans, while approximately 53% of the peer group's assets were loans; total deposits were somewhat comparable. Management attributes this variance to the bank's efforts to meet the community's demand for agricultural loans.

The following chart shows the net loan-to-deposit ratios since the previous examination:

3/95	6/95	9/95	12/95	3/96
70.16%	74.79%	76.40%	68.74%	68.93%

As the preceding chart indicates, the bank's loan-to-deposit ratio has been at a reasonable level since the previous examination. The most significant decline noted from the September, 1995 to December, 1995 quarters was due to a 7% increase in total deposits, while net loans only

increased by 4%. The bank's loan-to-deposit ratio is considered reasonable, given the bank's size, financial condition, and assessment area credit needs.

Lending in Assessment Area

The bank's summary of its lending activity revealed that the majority of the bank's consumer, mortgage, and commercial/agricultural lending activity continues to be within the bank's assessment area. The bank's reports, reviewed for lending activity since the previous examination, revealed that approximately 2,403 or 75.7% of the 3,173 total loans made between January 1995 and March 1996 were made within the bank's assessment area. The bank made 1,607 or 75.4% of the 2,132 consumer loans to borrowers residing within the assessment area and 699 or 77.8% of the 898 commercial/agricultural loans to borrowers having businesses or farms located within the assessment area. Additionally, 97 or 67.8% of mortgage loans originated by the bank were for the purpose of purchasing, constructing, or improving residences located within the bank's assessment area.

The examination loan sample revealed the following distribution:

LOAN TYPE	TOTAL SAMPLED	WITHIN THE LOCAL DELINEATED COMMUNITY	PERCENT OF TOTAL
Real Estate Mortgage	10	4	40%
Consumer Installment	20	16	80%
Credit Cards	10	8	80%
Home Equity	10	6	60%
Overdraft Protection	10	9	90%
Single Payment	20	15	75%
Commercial/Agricultural	20	14	70%

The examination loan sample further supports the fact that the majority of the bank's loan activity is conducted within the assessment area. Although the percentage of real estate mortgage loans (40%) made within the assessment area appears unfavorable, according to the above sample, consideration is given to the fact that many of these loans were made in areas bordering the bank's assessment area.

Based upon this review and the information provided by management, the bank's performance in making loans within the assessment area is satisfactory.

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

A portion of the bank's assessment area is located within a MSA. A review of the bank's 1995 HMDA data, which shows lending activity in the MSA portion of the bank's assessment area, revealed that loans to low- or moderate-income individuals comprised 43% of the total loans made within the assessment area. According to the census data, low- or moderate-income families account for approximately 37% of the total families in the bank's assessment area.

According to the Community Lending Analysis System (CLAS) from the Federal Reserve Board of Governors, the nonmetropolitan median family income for the State of Michigan is \$27,894. An analysis of a sample of loans made since the previous examination, which had borrower income information available, revealed the following distribution of loans to borrowers of different income levels:

LOAN TYPE	LOW-INCOME \$000's/Number	MODERATE- INCOME \$000's/Number	MIDDLE- INCOME \$000's/Number	UPPER-INCOME \$000's/Number
Real Estate	\$5,350/1	\$0/0	\$86,500/2	\$551,538/6
Installment	\$4,341/2	\$27,800/6	\$37,411/5	\$49,629/7
Credit Cards	\$300/1	\$6,500/4	\$2,000/2	\$3,000/3
Home Equity	\$0/0	\$3,000/1	\$14,000/2	\$89,700/6
Overdraft Protection	\$500/1	\$8,500/5	\$0/0	\$2,500/1
Single Payment	\$3,923/2	\$18,400/2	\$2,900/2	\$46,390/12
Total	\$14,414/7	\$64,200/18	\$142,811/13	\$742,757/35

As the preceding chart illustrates, the majority of the lending was to upper-income (35 loans) or moderate-income (18 loans) borrowers. The majority of the dollar volume was to upper-income (\$742,757) or middle-income (\$142,811) borrowers. The loan sample reveals that 18 or 25% of the 73 loans were granted to moderate-income borrowers, while moderate-income families comprise about 18% of the assessment area. This analysis further indicates a reasonable level of lending among borrowers of different income levels.

Management stated that the bank's primary commercial borrowers are smaller retail-oriented businesses. In addition, management stated the average revenue of farms in the area is approximately \$200,000. A sample of commercial/agricultural loans was performed to ascertain whether the bank was lending to businesses and farms of different sizes. Of the 16 loans sampled (with current annual revenue information available), borrowers' revenues ranged from \$48,000 to

\$413,000. The June 30, 1995 Consolidated Report of Financial Condition revealed that the bank had 279 outstanding loans (totaling \$8.3 million) or an average loan amount of approximately \$29,760 to small businesses on its loan portfolio. In addition, the report revealed 713 outstanding agricultural loans (totaling \$24.6 million) or an average loan amount of about \$34,553 to small farms. Management's comments were supported by the examiners' reviews which indicated the bank's commercial/agricultural lending activity is primarily to small businesses and farms.

The distribution of the bank's lending activity reflects a reasonable penetration among individuals of different income levels, and businesses and farms of different sizes.

Geographic Distribution of Loans

The bank's assessment area consists of five BNA's and seven census tracts within portions of Gratiot, Midland, and Saginaw Counties. Two or 17% of the census tracts and BNA's are considered moderate-income areas. A review of the bank's 1995 HMDA data revealed that the bank received 152 applications from residents within the MSA. Of the 152 applications, 112 or 74% loans were originated. Sixteen or 14.3% of the 112 loans were made to borrowers residing within the two moderate-income census tracts. This analysis compares favorably to the percentage of moderate-income areas within the assessment area.

The examiners reviewed the bank's reports (sorted by township codes) of loans made since the previous examination. The loan reports revealed that of the total 2,403 loan applications approved within the bank's assessment area, 303 or 12.6% were received from moderate-income areas. Further, 223 or 13.9% of the total consumer loans approved within the assessment area were made to borrowers residing in a moderate-income census tract. It was also noted that 69 or 9.9% of the total commercial loans made during the review period were made to businesses or farms located in a moderate-income census tract within the assessment area. In addition, 11 or 11.3% of the 97 real estate loans originated within the bank's assessment area were to borrowers in moderate-income areas. According to this analysis, on average, approximately 12% of the bank's lending activity within the assessment area is conducted within moderate-income census tracts, which compares favorably to the fact that moderate-income areas comprise approximately 17% of the entire assessment area.

The geographic distribution of loans is dispersed throughout the assessment area and is considered reasonable. No particular areas were noted that do not have loan penetration.

Response to Complaints

No CRA-related complaints were received by the bank since the previous examination.