PUBLIC DISCLOSURE

August 11, 1997

COMMUNITY REINVESTMENT ACT
PERFORMANCE EVALUATION

Valley Bank of Arizona
DSBB# 12-04-0156-0000

3550 North Central Avenue, Suite 150
Phoenix, Arizona 85012

FEDERAL RESERVE BANK OF SAN FRANCISCO
101 MARKET STREET
SAN FRANCISCO, CALIFORNIA 94105

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. 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 Community Reinvestment Act (CRA) performance of **Valley Bank of Arizona** prepared by the **Federal Reserve Bank of San Francisco**, the institution's supervisory agency, as of **August 11, 1997**. 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 CRA RATING: This institution is rated satisfactory.

The bank has met the standards for satisfactory performance in three of the five performance criteria evaluated and exceeded standards for the fourth. The were no written complaints received by the bank about its CRA performance; therefore, this fifth criteria was not evaluated. The bank's lending within its assessment area meets standards for satisfactory performance and its lending to businesses of different income levels shows that the bank is penetrating and meeting the needs of the small business community. Moreover, the geographic distribution of loans shows a high percentage of lending in low- and moderate-income census tracts. This distribution exceeds standards for satisfactory performance. The bank's loan-to-deposit ratio is comparable to its peers and the trend shows a steady growth over the past five quarters.

DESCRIPTION OF INSTITUTION:

Valley Bank of Arizona opened for business on March 11, 1996, and is wholly owned by Valley Bankcorp. Over the past 17 months, the bank's asset size has grown to $18.5 million. The bank offers a wide range of both consumer and business oriented deposit products and targets its lending activities to small businesses. As of June 30, 1997, over 80% of the bank's loan portfolio consisted of commercial loans. The remainder is split between real estate and consumer loans. Currently, the bank has one branch located in Phoenix's financial district.

The bank underwent a change of direction in February 1997. During its first year of operation, the bank focused on its image in the community and involved itself with shared national credits as a way of strengthening its loan portfolio. Direct lending consisted primarily of commercial real estate secured loans. However, since February, there has been a shift in focus to small business lending (equipment and working capital purposes) and a new SBA lending program.

The bank is in the process of hiring additional loan officers to develop the small business market. Previously, loan officers concentrated their activities in commercial real estate. With the bank's new focus, the new loan officers have expanded their efforts beyond commercial real estate and are looking to the small business community for new lending opportunities.

There are no legal impediments that would limit the bank's lending activities or that would adversely affect the bank's ability to meet various community credit needs. This is the first Community Reinvestment Act evaluation for this institution.

DESCRIPTION OF ASSESSMENT AREA:

Valley Bank's assessment area covers approximately 30 square miles and includes the downtown business district, the Sky Harbor Airport Industrial Zone, Paradise Valley and eastern Scottsdale.

According to the 1990 census, the population within the assessment area was 410,807 representing 18% of the population of the metropolitan Phoenix area. The assessment area includes all income levels of census tracts, with the following distribution: 24% low-income, 35% moderate-income, 23% middle-income and 18% upper-income census tracts. As of 1/1/97, the population of the Phoenix metropolitan area has grown to 2,528,425.

Areas of the Phoenix economy which have been targeted for growth include biotechnology, business services, health services, and high-technology industries and software.[1] Some of the major employers include Motorola Inc., Honeywell,

[1] The Best Place to Live and Work, Employment Review, Annual 1996.

Intel, Samaritan Health System, American Express and the Dial Corp. Historically, Phoenix has consistently experienced positive job growth[2] and is ranked number two in the nation for job growth among large cities.[3]

During this examination, contacts were made with various community representatives focusing in the area of economic development. They indicated that there is rapid growth in the number of small businesses especially in the service and retail industries. These types of businesses have a need for both start-up and working capital loans, especially in amounts of $100,000 or less. Several community organizations have specialized loan programs to assist financial institutions in meeting these credit needs while mitigating all or part of the credit risk involved.

The bank's assessment area offers many opportunities for small business lending. There are no impediments within the community that would prevent the bank from making loans or investing within its assessment area.

CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA:

The evaluation of Valley Bank of Arizona's performance under the Community Reinvestment Act includes a review of the bank's commercial loan portfolio as well as an in-depth study of its assessment area. Information was collected from the bank, community contacts, and the 1990 Census to draw conclusions regarding the local economy, credit demand, and the demographic characteristics of the assessment area. Examiners considered this information in assessing the bank's credit extensions as it relates to the bank's record of helping to meet the credit needs of its community.

In order to evaluate the bank's lending performance, examiners reviewed 108 business purpose loans to determine the number and dollar amount of loans made inside and outside of the bank's assessment area. Only those loans that were extended inside the assessment area were analyzed for purposes of determining the revenue size of the businesses and geographic distribution of loans. The bank's performance under four assessment criteria was determined using the results of this analysis: Assessment Area Concentration, Lending by Business Revenue, Geographic Distribution of Loans and Loan-to-Deposit Ratio. There were no CRA complaints received by the bank; therefore, this fifth criteria was not evaluated.

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[2] Taken from "The Best Places to Live and Work," Employment Review, August 1996. Article states in the context of "...in 37 out of the past 40 years, Phoenix has experienced positive job growth."

[3] The Business Journal of Phoenix, June 16, 1997

LENDING IN ASSESSMENT AREA:

As illustrated by the chart below, of the bank's 108 small business loans, 66 (61%) were made within Valley Bank's assessment area. In addition, the dollar volume of these loans represents $13,335,973 or 56% of the bank's total lending volume of $23,918,863. This indicates that most of the bank's lending is occuring within the assessment area.

The examiners further analyzed the distribution of loans by categorizing small business loans into two loan products: real estate secured and non-real estate. As depicted in Appendix A, non-real estate secured small business loans totaled 82, with 57 (70%) falling within and 25 (30%) falling outside the assessment area. The dollar volume of these loans total $16,141,154 with $10,092,264 (62%) being extended inside the assessment area. There were 26 small business loans secured by real estate, with nine (35%) extended inside and 17 (65%) extended outside the assessment area.

The large number of real-estate secured loans outside of the assessment area is primarily due to the borrowers brought in by the bank's former loan officers who came from other financial institutions located outside of the bank's assessment area. As a result, most real estate loans that are in the bank's portfolio are for properties located outside of its assessment area. Nonetheless, this loan activity is reasonable for a de novo institution that is in the process of forming its loan portfolio. Moreover, given Valley Bank's small assessment area as compared to the MSA (Metropolitan Statistical Area) and the bank's former senior managements' strategy of purchasing shared national credits, a large percentage of the bank's loans were extended outside the assessment area.

With its new management team, Valley Bank has moved its focus from commercial real estate lending to financing the credit needs, such as, working capital and equipment financing for small businesses located within its assessment area. The president indicated that he views his typical customer as someone needing loans of $250,000 and less, either as a line of credit or a commercial-term loan. The bank's shift in business strategies has resulted in the majority of its loans being extended inside the assessment area and, therefore, meets standards for satisfactory performance for this criteria.

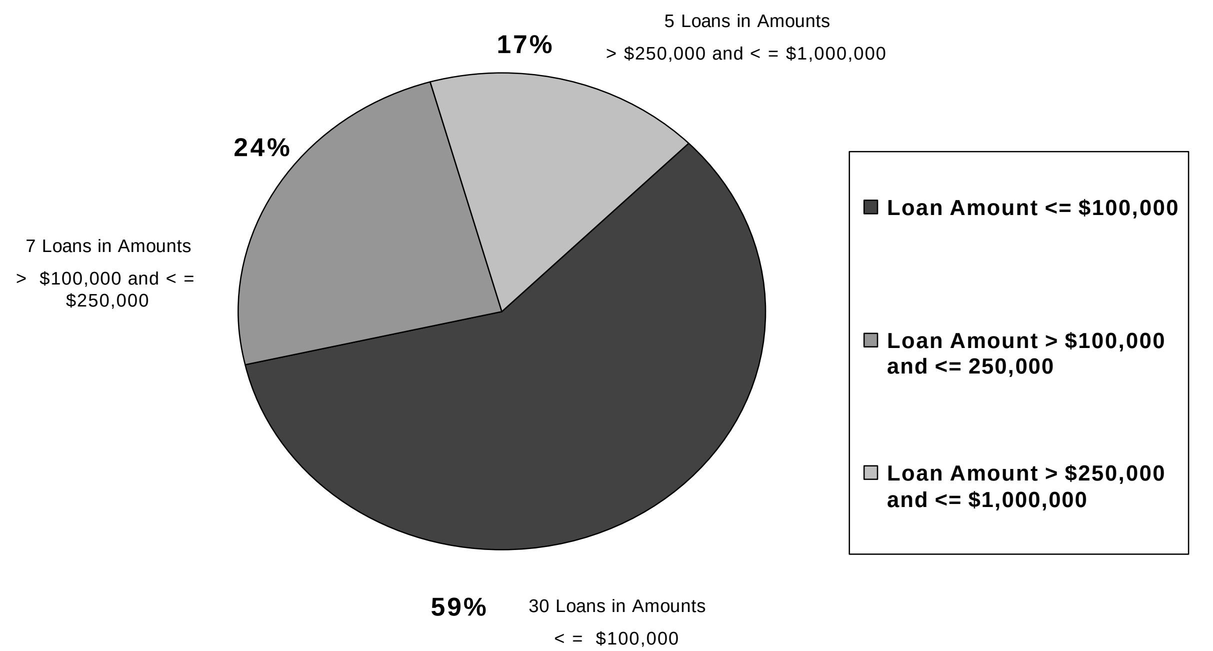
<u>LENDING BY BORROWER INCOME AND BY BUSINESS REVENUE</u>:

Forty-four percent of the loans extended by the bank inside its assessment area were to businesses with gross annual revenues of less than $1 million[4]. This percentage is reasonable given the young age of this institution and its previous management's business strategy. Furthermore, an analysis of the bank's lending to large businesses revealed that lending of this type is limited to a few core clients, with multiple loans to each client. Due to the bank's relatively small loan portfolio, the loans to the large businesses have had a relatively great impact on the number and dollar amount extended to businesses of different sizes, by giving the appearance that the bank has a large business customer base (Refer to Appendix B).

[4]Small businesses are defined as those businesses that had annual gross revenues of less than $1 million.

An analysis of Valley Bank's small business loan[5] portfolio showed that 83% of the loans extended to small businesses were made in amounts at or below $250,000, with 59% in amounts of $100,000 or less (see chart below). According to a commercial loan specialist for the City of Phoenix, there is a demand for loans in amounts less than $100,000 within the small business community. In discussing financial institutions in the Phoenix area, he stated that "Most commercial lenders prefer to make loans in the $1 million range."

Distribution of Small Business Loans within the Assessment Area by Loan Amount



Considering that the number of loans to large businesses resulted from multiple loans to a few core clients, and that the lending level indicates responsiveness in meeting the credit needs of small businesses through extension of small dollar loans, the bank meets standards for satisfactory performance in the borrower profile criterion.

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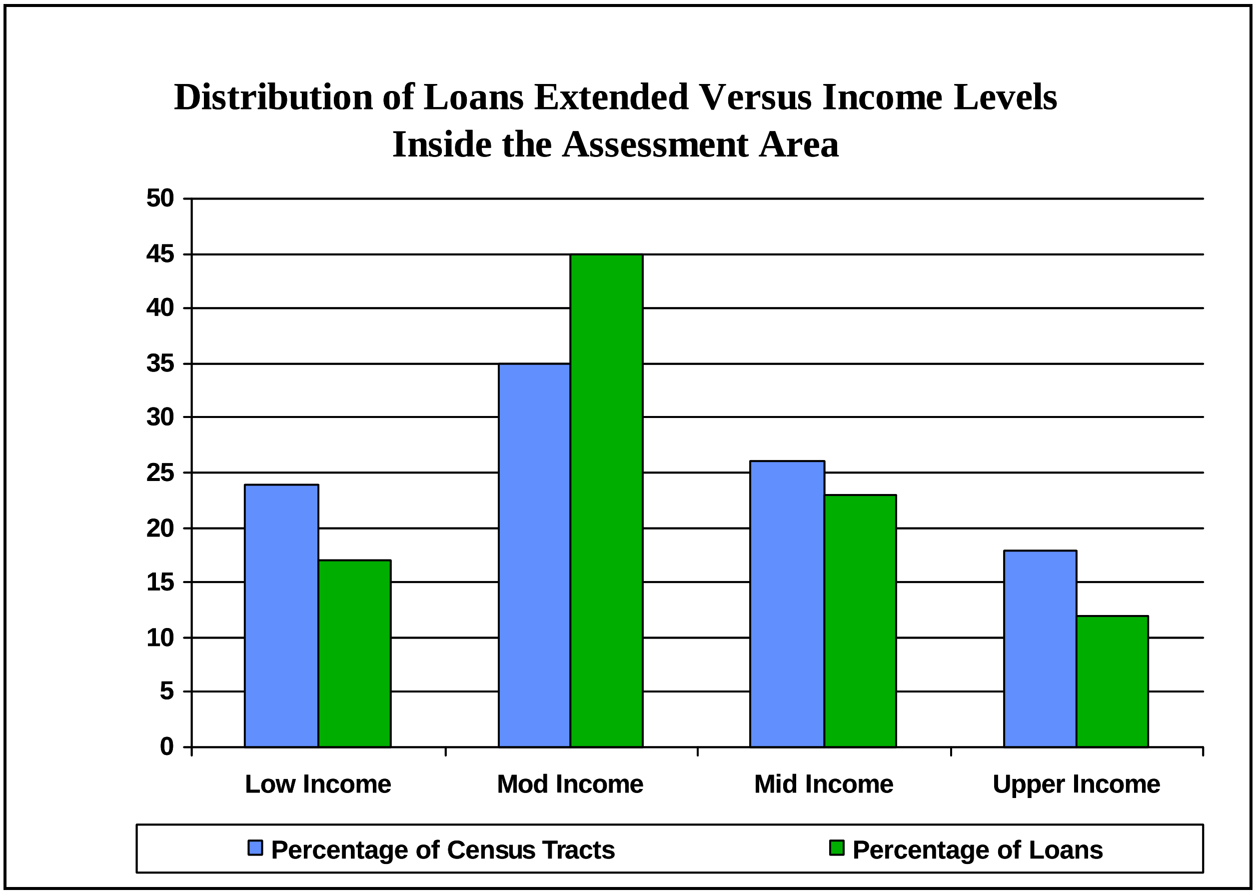
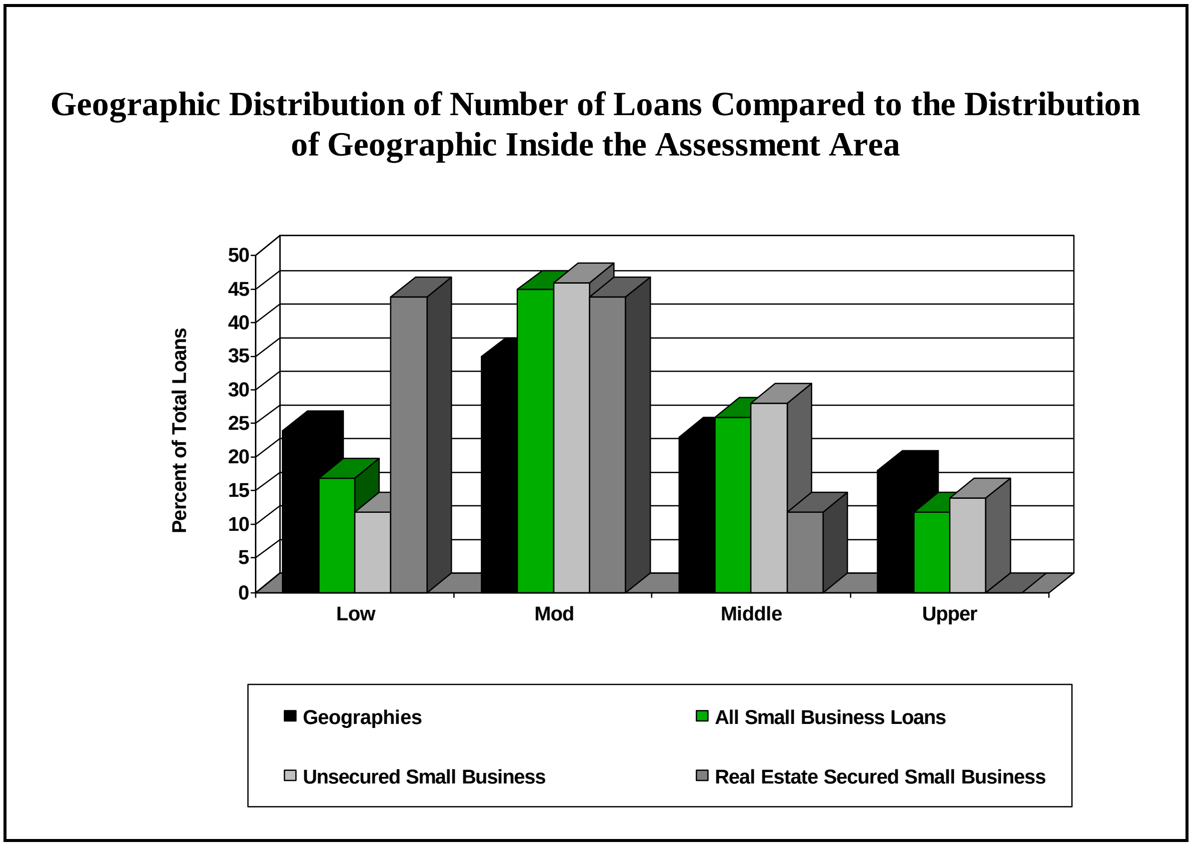
[5] Small business loans are defined as those that are less than or equal to $1 million in amount.

GEOGRAPHIC DISTRIBUTION OF LOANS:

An evaluation of the geographic distribution of loans extended throughout the bank's assessment area shows that the bank has penetrated low- and moderate-income census tracts.



The chart above shows the distribution of the bank's loan portfolio within its assessment area. Of the loans made within the assessment area, 11 (17%) were made in low-income, 29 (45%) in moderate-income, 17 (26%) in middle-income, and 8 (12%) in upper-income census tracts. The bank's assessment area consists of 24% low-income, 35% moderate-income, 23% middle-income and 18% upper-income census tracts. A review of the bank's lending history in its assessment area shows that 62% of the small business loans were extended in low- and moderate-income census tracts. The geographic distribution of small business loans compares favorably to the distribution of low- and moderate-income census tracts in the assesment area. The bank's lending record is particularly strong in moderate-income areas.

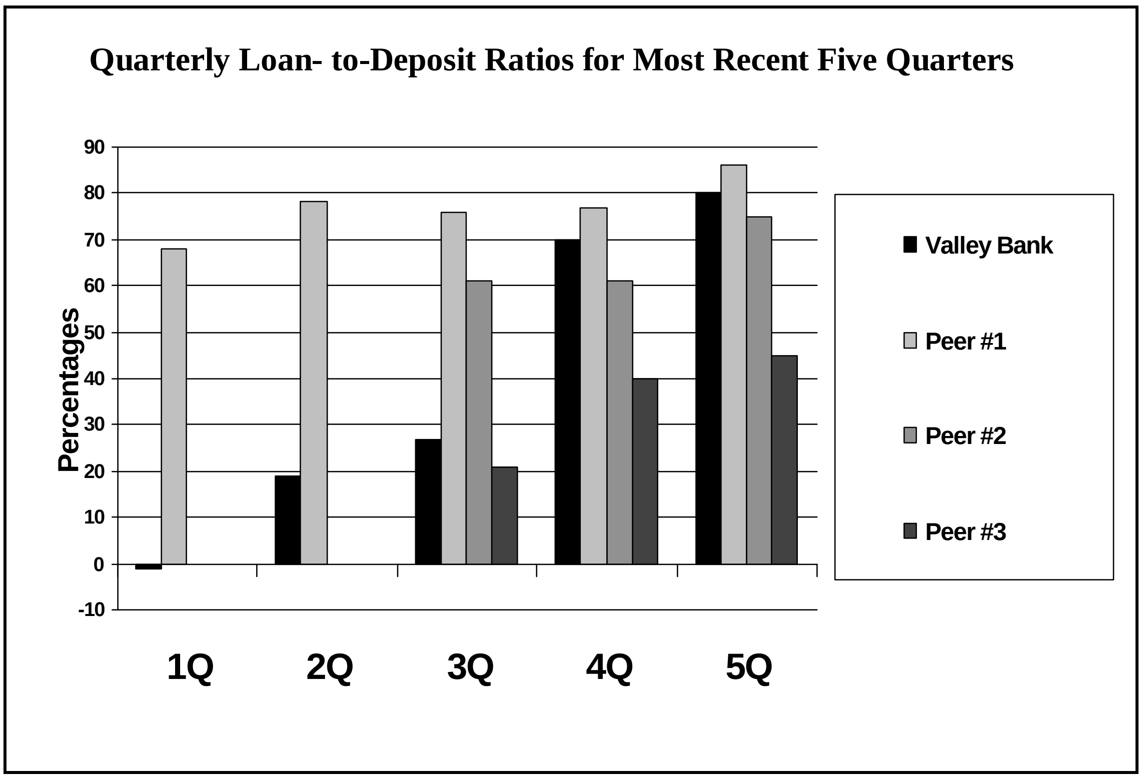


The assessment area is unusual in that commercial and residential areas are intermixed. It is common to see single family residential units next to a multi-story office complex. Although this causes a dispersion of businesses throughout the assessment area, small businesses tend to be concentrated in low- and moderate-income census tracts. Therefore, the bank's high level of lending in low- and moderate-income (LMI) areas benefits both small businesses and individuals residing in LMI areas. For these reasons, Valley Bank exceeds standards for satisfactory performance under this performance criteria.

LOAN TO DEPOSIT RATIO:

Valley Bank's current loan-to-deposit ratio is similar to that of its peers and has been showing steady growth since the bank opened. For this analysis, three peer banks were selected based on their asset size, business focus, branch network, and length of time in business. A national peer was not used for this comparison because the bank's de novo status reduces the usefulness of a national comparison. Furthermore, there were similarly situated institutions available in the Phoenix community.

Examination procedures require the bank's average loan-to-deposit ratio to be calculated using all quarters reported since the previous examination. As illustrated in the graph below, if all five reporting quarters since the bank opened on 3/11/96 were used for comparison, Valley Bank of Arizona's loan-to-deposit ratio would fall far below that of its closest peer. This five-quarter analysis is not considered valid for two reasons. First, one peer bank has been in operation for over eight years and has an established client base. Second, the other two peers opened for business after Valley Bank and have only reported in three of the five quarters used for this comparison. Because of the de novo status of the bank's two peers, a more appropriate measure would be to compare the most recent three quarters and place the greatest weight on the most recent two quarters. This methodology places more emphasis on the bank's current loan-to-deposit trend rather than during the start-up period when the bank had few deposits and



limited loan activity.

An analysis of the most recent three quarters shows that the bank's loan-to-deposit ratio (59%) has risen although it is still low in comparison with its closest peer (80%). This trend is reasonable because the bank is still in the process of developing its client base and loan portfolio. At this period, the bank falls between the other two banks. As the bank expanded, the upward trend has continued, particularly in the most recent two quarters. As of 6/30/97, Valley Bank increased its loan-to-deposit ratio to 75%.

The bank's lending performance during the most recent two quarters, coupled with the bank's young age and steady growth trend in its loan-to-deposit ratio since inception, shows that it is comparable to its peers and meets standards for satisfactory performance in this area.

RESPONSE TO COMPLAINTS:

The bank has not received any complaints about its CRA performance.

COMPLIANCE WITH FAIR LENDING LAWS AND REGULATIONS:

No violations of the substantive provisions of the antidiscrimination laws and regulations were found during this examination.