

## **PUBLIC DISCLOSURE**

October 20, 1997  
Date of Evaluation

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### **COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION**

State Bank of Alcester  
Name of Depository Institution

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094600300000  
Identification Number of Institution

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Alcester, South Dakota  
Address of Institution

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Federal Reserve Bank of Minneapolis  
90 Hennepin Avenue  
Minneapolis, Minnesota 55480-0291

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.

## 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 the 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 CRA performance of State Bank of Alcester, Alcester, South Dakota, prepared by the Federal Reserve Bank of Minneapolis, the institution’s supervisory agency, as of October 20, 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.”

Several factors support rating the bank’s CRA performance satisfactory. First, the bank’s lending to borrowers of different income levels and farms of various sizes is reasonable. Second, the bank’s net loan-to-deposit ratio is reasonable and has increased slightly since the previous evaluation. Finally, the bank’s lending activity is concentrated in the assessment area.

## **DESCRIPTION OF INSTITUTION**

Based on its size and financial condition, the bank is able to meet the credit needs of its assessment area effectively. The bank was rated outstanding in helping to meet the credit needs of its community at its previous CRA evaluation. The bank operates a full-service office in Alcester, South Dakota, and has no branch offices. The bank also owns and operates three automated teller machines (“ATM”), one in Alcester and two in Beresford, South Dakota. At these ATMs, users can withdraw, but cannot deposit funds. The bank has not opened or closed any branches since the last evaluation.

According to the bank’s September 30, 1997, Report of Condition (“ROC”), the bank’s assets totaled approximately \$59.7 million. Its September 30, 1997, ROC indicates the bank’s major loan category is agricultural lending, which constituted approximately 51% of its loan portfolio. The balance of the bank’s loan portfolio is composed of 19% commercial, 15% residential real estate, 14% consumer, and 1% other loans. The composition of the bank’s loan portfolio appears to reflect the level of demand for the specific types of loans in the assessment area.

The bank offers a variety of loan products to fulfill the needs of residents, businesses, and farms within its assessment area. Its loan products include conventional agricultural, commercial, consumer, and residential real estate loans. With respect to the latter loan category, the bank offers residential real estate loans for one- to four-family dwelling units, housing rehabilitation, and home improvement loans. It also offers home equity lines of credit.

In addition to offering conventional loan products, the bank participates in federal loan programs sponsored by the Farm Service Agency, Small Business Administration, Federal Housing Administration, and Department of Veterans Affairs. It also offers loans through the following state agencies: the South Dakota Department of Agriculture (“SDDA”) and the South Dakota Housing Development Authority (“SDHDA”). More specifically, the bank participates in SDDA’s Loan Participation Program (“LLP”), Value Adding Livestock Underwriting Program, and Beginning Farm Bond Program (“BFBP”) and in SDHDA’s First-Time Homebuyer Program (“FHP”), Mortgage Assistance Program (“MAP”), Mortgage Assistance Grant Program (“MAGP”), and Cooperative Home Improvement Program (“CHIP”). The SDDA’s LLP and BFBP are low interest rate loan programs. Through FHP and CHIP, the bank offers below-market-rate mortgage and home improvement or renovation loans, respectively. The CHIP is available to successful applicants whose incomes are 95% or less of the applicable state or county median family income. The MAP and MAGP provide down payment and closing cost assistance. Finally, the bank participates in government-guaranteed student loan programs.

The bank’s loan products appear appropriate to fulfill the credit needs of residents, businesses, and farms in its assessment area.

## **DESCRIPTION OF STATE BANK OF ALCESTER’S ASSESSMENT AREA**

The bank has defined its assessment area as portions of Union and Lincoln counties in extreme southeastern South Dakota and portions Plymouth and Sioux counties in extreme northwestern Iowa. Based on the 1990 U.S. Census, the population for the assessment area is approximately 16,652. The section of the assessment area in Lincoln County consists of census tract 104, which is part of the Sioux Falls, South Dakota, Metropolitan Statistical Area (“MSA”). This census tract is well south of Sioux Falls and does not include the city. In addition to MSA census tract 104, the assessment area includes non-MSA

census tracts 201 and 202 in Union County, block numbering area (“BNA”) 9703 in Plymouth County, and BNA 9704 in Sioux County.

As previously noted, the bank’s only office is in Alcester, which is located in census tract 201. Other communities in the assessment area include Beresford, Elk Point, Big Springs, and Hudson in South Dakota, and Akron, Chatsworth, and Hawarden in Iowa.

CRA divides income levels into four categories: low, moderate, middle, and upper. The categorization of a borrower or geography’s income is determined relative to either the statewide nonmetropolitan median family income or the MSA median family income. For classification purposes, the appropriate median family income depends on whether a borrower or geography is in the MSA or the nonmetropolitan areas of South Dakota or Iowa. Low-income individuals have incomes of less than 50% of the statewide nonmetropolitan or MSA median family income, while moderate-income individuals have incomes of at least 50% but less than 80% of the relevant geography’s median family income. The regulation defines a middle-income individual as one with an income at least 80% but less than 120% of the statewide nonmetropolitan or MSA median family income. An individual with an income that is 120% or more of the statewide nonmetropolitan or MSA median family income is considered an upper-income person. Borrower incomes are classified based on the 1997 median family income for the relevant geographical area. Census tracts and BNAs are classified using similar categories based on the level of the median family income in the geography; however, geography incomes are classified based on 1990 median family income data.

Based on 1990 census data, the following table shows the median household and family incomes for the assessment area, South Dakota and Iowa’s nonmetropolitan areas, and the MSA.

<b>1990 MEDIAN INCOMES</b>		
	Household Median Income	Family Median Income
Assessment Area	\$22,677	\$27,206
South Dakota Nonmetropolitan Areas	\$20,736	\$25,547
Iowa Nonmetropolitan Areas	\$24,256	\$29,303
MSA	\$27,843	\$34,101

As illustrated above, the assessment area’s household and family median incomes fall between the nonmetropolitan statewide median incomes for South Dakota and Iowa. On average, households and families in the assessment area have incomes higher than households and families in South Dakota’s rural areas. As compared to Iowa’s rural households and families, however, people in the assessment area generally have lower incomes. As the data set forth in the table show, the assessment area’s median household and family incomes are much lower than the comparable figures for the MSA. According to the 1990 census data, 55% of the assessment area’s residents live in South Dakota while 45% live in Iowa. Similarly, the percentage of assessment area households and families residing in South Dakota is 55% and 54%, respectively.

There are 6,311 households and 4,550 families in the assessment area. The following table summarizes the distribution of household and family income for the assessment area.

<b>DISTRIBUTION OF ASSESSMENT AREA POPULATION BY INCOME LEVEL</b>				
<b>Unit of Measure</b>	<b>Low Income</b>	<b>Moderate Income</b>	<b>Middle Income</b>	<b>Upper Income</b>
Households Compared to Median Household Income	23.6%	17.2%	22.1%	37.1%
Families Compared to Median Family Income	17.2%	21.2%	27.8%	33.8%

The percentage of assessment area low-income households and families is comparable to the representation of such households and families in South Dakota and Iowa's nonmetropolitan areas. In South Dakota's nonmetropolitan areas, 19.5% of the families and 23.6% of the households have low incomes. In Iowa's nonmetropolitan areas, 17.5% of the families and 22.9% of the households have low incomes. With respect to middle-income households and families, the assessment area's percentages are slightly higher than both South Dakota and Iowa's nonmetropolitan areas.

The following table shows the percentages of households and families in the assessment area that have incomes below the poverty level.

	<b>Households with Incomes Below Poverty Level</b>	<b>Families with Incomes Below Poverty Level</b>
Assessment Area	13.3%	8.6%
South Dakota Nonmetropolitan Areas	17.9%	13.7%
Iowa Nonmetropolitan Areas	12.5%	8.8%

The assessment area's figures for household and family incomes below the poverty level are comparable or lower than those of the nonmetropolitan areas of both states represented in the assessment area. According to the 1990 census, the unemployment rate for the assessment area was 2.4%. This rate is much lower than South Dakota and Iowa's nonmetropolitan area's unemployment rates of 4.3% and 4.4%, respectively.

Each assessment area census tract and BNA is designated as a middle-income geography based on comparison to the relevant state or MSA median family income. Although all the geographies are middle income, the median family income varies significantly between them. Tract 201, which includes the bank, has a median family income of \$25,109 and median household income of \$19,891. This tract would be classified moderate income if it were compared to MSA median family income. The other tract in Union County, tract 202, has the highest median family income in the assessment area at \$29,762 and the second highest median household income.

According to bank management and the community contact, agriculture is the area's main industry. Major farm products consist of corn and soybeans. According to the South Dakota Agricultural Statistics Service, Union County ranked fifth in the state for corn and soybean production for 1996. Also in 1996, Lincoln County's state rankings were third in corn and second in soybean production. Based on a 1992 agricultural census, Union County has 560 farms that have an average farm size of 463 acres. The area's agricultural sector has been strong through the 1990s because of generally high crop yields.

According to the community contact, Alcester's economy is strong. To support this assertion, the contact noted that local sales tax revenues have increased in recent years, reflecting a higher sales volume of goods

and services in the area. Major employers in the community include the school district, a nursing home, a meat packing company, a cleaning service, a manufacturer, and the bank.

Since a primary need in the community is residential housing, the bank was involved in reinstating the Alcester Development Company's ("ADC") development of the Numsen Addition housing project. The ADC has completed the infrastructure development for 22 lots that will be made available soon. It plans to develop 17 additional lots in the future. ADC developed this area to provide lots for single-family and multifamily housing units. During the summer of 1997, seven single-family dwellings were constructed in the addition.

According to the 1990 census, 86% of the assessment area's homes were one-unit structures. Dwellings consisting of two to four units accounted for 4% of the assessment area's housing units. Likewise, dwellings consisting of five or more units accounted for 4% of the assessment area's housing units. Finally, mobile homes represented 5% of the assessment area's housing structures. As a percentage of housing units in the assessment area, 67% were owner-occupied, 25% were rental, and 8% were vacant.

Examiners contacted a representative of local government as part of the bank's CRA evaluation. The community contact provided information regarding the local business and agricultural economic conditions. Examiners used information from this contact as well as information from bank management to evaluate the bank's CRA performance.

## CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA

The bank's performance in meeting the assessment area's credit needs is satisfactory. Much of the analysis on the following pages is based on a statistical sample of 135 consumer and 100 small farm loans originated by the bank during the six months preceding the evaluation. It is also based on a statistical sample of 46 residential real estate loans originated during the 12 months preceding the evaluation. In assigning the overall rating, greatest weight was placed on the bank's level lending to borrowers of different income levels and farms of different sizes. This factor most closely measures the bank's efforts to meet the credit needs of all segments of its community.

### LOAN-TO-DEPOSIT RATIO ANALYSIS

The bank's net loan-to-deposit ratio meets the standards for satisfactory performance. Based on quarterly ROC data, the bank's average net loan-to-deposit ratio since the previous evaluation is 69%. The bank's quarterly average net loan-to-deposit ratio at the previous evaluation was 66%.

The following chart, based on quarterly ROC data since the previous evaluation, shows that the bank's net loan-to-deposit ratio has ranged from 63% to 76%.

<b>DATE</b>	<b>NET LOANS (IN THOUSANDS)</b>	<b>DEPOSITS (IN THOUSANDS)</b>	<b>NET LOAN-TO-DEPOSIT RATIO</b>
June 30, 1996	\$32,092	\$46,811	69%
September 30, 1996	\$34,768	\$49,148	71%
December 31, 1996	\$33,689	\$50,801	66%
March 31, 1997	\$32,433	\$51,424	63%
June 30, 1997	\$34,611	\$50,373	69%
September 30, 1997	\$38,078	\$50,295	76%

Since June 30, 1996, the bank's net loans and deposits have fluctuated, reflecting the normal business cycle of the assessment area's predominantly agricultural economy. The bank's net loan data does not include a number of residential real estate loans sold to the secondary market since the previous evaluation. If these loans were included in the net loan data, the bank's net loan-to-deposit ratio would be higher. Between September 30, 1996 and 1997, net loans increased approximately 10% while deposits increased only 2%. According to bank management, the net loan growth is a result of the bank's aggressiveness in seeking new loan customers and providing new credit products.

According to the June 30, 1997, Uniform Bank Performance Report ("UBPR"), the bank's net loan-to-deposit ratio was 68.71%, which ranked the institution in the 55th percentile of its national peer group. As of the same date, the bank's net loan-to-assets ratio was 61.42%. The average net loan-to-assets ratio for South Dakota banks with total assets between \$25 million and \$100 million was 60.91%. This data show that the bank dedicates approximately the same percentage of its assets to net loans as similarly sized banks operating in the state.

The bank is the third largest financial institution operating in or near the assessment area. The bank's average net loan-to-deposit ratio is lower than the ratios of its two larger competitors; nonetheless, it appears reasonable in light of the ratios for all banks operating in or near the assessment area. Based on the quarterly ROC data from June 30, 1996, to June 30, 1997, the following table identifies the asset size and quarterly average net loan-to-deposit ratio for the bank and its competitors.

<b>BANK AND LOCATION</b>	<b>TOTAL ASSETS</b> (AS OF JUNE 30, 1997) (IN THOUSANDS)	<b>QUARTERLY AVERAGE</b> <b>NET LOAN-TO-DEPOSIT</b> <b>RATIO</b>
State Bank of Alcester Alcester, South Dakota	\$56,347	68%
Peoples Bank and Trust Rock Valley, Iowa	\$68,144	80%
Valley Bank National Association Elk Point, South Dakota	\$61,306	81%
The First National Bank of Akron Akron, Iowa	\$37,823	67%
Farmers State Bank Hawarden, Iowa	\$37,003	63%
First Midwest Bank Centerville, South Dakota	\$33,266	71%
Iowa State Bank Ireton, Iowa	\$26,023	46%
First Sate Bank Hawarden, Iowa	\$20,090	77%
State Bank of Hudson Hudson, South Dakota	\$15,690	79%

As the data in the table illustrate, five of the eight banks listed have higher average quarterly net loan-to-deposit ratios than the subject bank. The other three banks have ratios that are equal to or lower than the bank's ratio.

The number of financial institutions operating in or near the bank's assessment area creates a very competitive credit market for the types of loans offered by the bank. There is a branch of a large regional financial institution and a Farm Credit Services office in Beresford, which is approximately 10 miles from Alcester. The bank also competes against nonbank lenders, such as farm equipment and automobile dealers. The assessment area's proximity to Sioux Falls, which is 40 miles north of Alcester and is the retail and commercial center for the region, means that the bank faces competition from numerous financial institutions operating in that city.

As reflected in the competitor data, it appears the demand for credit in the assessment area is strong. It is also apparent that the local banks are willing to extend credit to fulfill the needs of local residents, farms, and businesses. The community contact confirmed that there are no unmet credit needs in the assessment area. Therefore, based on the bank's net loan-to-deposit ratio relative to local competitors as well as its statewide and national peers, the bank's net loan-to-deposit ratio is reasonable and meets the standards for satisfactory rating.

#### DISTRIBUTION OF CREDIT WITHIN THE ASSESSMENT AREA

The distribution of the bank's loans within the assessment area is reasonable. A review of the statistical sample of consumer, residential real estate, and small farm loans originated by the bank reveals that it extends a majority of its loans inside the assessment area. The bank's small farm loans are highly concentrated in the assessment area; this is particularly significant because 51% of the bank's loan portfolio is composed of agricultural loans. The following table shows the percentage of loans within the assessment area based on total number and dollar amount in each major loan category.

<b>LOANS IN THE ASSESSMENT AREA</b>		
<b>Major Loan Product Line</b>	<b>Total Number of Loans</b>	<b>Total Amount of Loans</b>
Consumer	71%	68%
Residential Real Estate	85%	75%
Small Farm	89%	91%

As shown in the table, the bank extends a significant majority of its loans to individuals and small farms within the assessment area. The data reveal that the bank extends many consumer loans to borrowers who reside outside the assessment area; bank management attributed this situation to the fact that some customers have moved from the area but continue to maintain a borrowing relationship with the bank. The concentration of the bank's consumer, residential real estate, and small farm loans in the assessment area has not changed significantly since the last evaluation.

Based on the concentrations of loans within the assessment area, the bank's lending performance meets this category's standards for satisfactory performance.

**LENDING TO BORROWERS OF DIFFERENT INCOME LEVELS AND TO BUSINESSES OF DIFFERENT SIZES**

The bank's level of lending to individuals of different incomes and to farms of different sizes meets the standards for satisfactory performance. As discussed previously, CRA classifies borrower income levels into four categories: low, moderate, middle, and upper.

As mentioned earlier, the data used to evaluate the bank's CRA performance is based on a statistical sample of consumer, residential real estate, and small farm loans originated before the evaluation. For purposes of evaluating the income distribution of the bank's consumer borrowers, however, the data proved inconclusive. Income data was available for only 29% of the consumer loans sampled; therefore, the information derived from the review of the bank's consumer loans is not a reasonable indicator of the bank's performance in this category. Income data for the bank's residential real estate loan borrowers was available for 85% of the sample loans. Therefore, the bank's performance for this category will be evaluated based solely on the residential real estate and small farm loan data.

The following table shows the percentage of residential real estate loans made to borrowers of different income levels.

<b>DISTRIBUTION OF LOANS IN THE ASSESSMENT AREA* BY BORROWER INCOME LEVEL</b>				
<b>Loan Type</b>	<b>Low Income</b>	<b>Moderate Income</b>	<b>Middle Income</b>	<b>Upper Income</b>
<b>RESIDENTIAL REAL ESTATE</b>				
Percentage of Number of Loans	18%	18%	40%	24%
Percentage of Amount of Loans	21%	21%	32%	26%
*Income level is determined based on the 1997 South Dakota nonmetropolitan median family income of \$34,500 for borrowers in census tracts 201 and 202 and the 1997 Iowa nonmetropolitan median family income of \$39,200 for borrowers in BNAs 9703 and 9704. Income level for borrowers in MSA census tract 104 is based on the 1997 MSA median family income of \$45,700.				

As shown above, the bank extended 36% of its residential real estate loans to low- and moderate-income borrowers. According to the 1990 census data, low- and moderate-income households and families comprise 40.8% and 38.4% of the assessment area population, respectively. More specifically, low- and moderate-income households represent 23.6% and 17.2% of the assessment area's population, respectively. The respective percentages for the assessment area's low- and moderate-income families are 17.2% and 21.2%. Based on the loan data, the bank's residential real estate lending to low- and moderate-income borrowers appears reasonable given the representation of such households and families in the assessment area.

Since the last evaluation, the bank increased both the relative number and dollar amount of residential real estate loans extended to low-income borrowers. At the last evaluation, the data showed that low-income borrowers received 15% of the number and 4% of the dollar amount of the bank's residential real estate loans; the bank's current performance shows improvement in both these categories for low-income borrowers. As of the last evaluation, the bank extended 22% of the number and 24% of the dollar amount of its residential real estate loans to moderate-income borrowers. The current data show that the bank's loan activity to moderate-income borrowers has declined slightly since the last evaluation. Nonetheless, the

increased loan activity to the assessment area's low-income residents is commendable and noteworthy in light of the competition in the area.

The bank offers several loan products that serve the credit needs of low- and moderate-income borrowers. First, the bank is willing to extend small consumer loans. Second, it offers SDHDA's FHP, MAP, MAGP, and CHIP loans. These programs typically benefit low- and moderate-income borrowers.

Reflecting the nature of the local agricultural market, all the sampled small farm loans were to operations grossing less than or equal to \$1 million in annual revenues. Small farm loans are loans with original amounts of \$500,000 or less; all of the bank's agricultural loan originations during the sample period were small farm loans. Of these loans, 92% were for amounts less than or equal to \$100,000, 6% were for loan amounts of more than \$100,000 and less than or equal to \$250,000, and 2% were for amounts of more than \$250,000 and less than or equal to \$1,000,000. The concentration of small farm loans in the bank's loan portfolio appears to reflect the bank's asset size, legal lending limit, and local agricultural market.

The bank is willing to extend loans to borrowers of different income levels and to farms of various sizes. Its residential real estate lending activity appears reasonable given the assessment area's demographics. Further, all the bank's small farm loans were to entities that have gross annual revenues of \$1,000,000 or less; however, this is expected given the agricultural market in which the bank operates. Given the bank's level of loans to low- and moderate-income borrowers as well as small farm loans to entities with gross annual revenues of \$1,000,000 or less, the bank meets this category's standards for satisfactory performance.

#### GEOGRAPHIC DISTRIBUTION OF LOANS

The distribution of the bank's loans in its assessment area is considered reasonable and meets the standards for satisfactory performance. As previously discussed, the bank's assessment area is composed of middle-income census tracts and BNAs; it does not have any low-, moderate-, or upper-income geographies. The following table shows the percentage of loan penetration in each of the bank's census tracts and BNAs.

<b>LENDING ACTIVITY BY GEOGRAPHY</b>						
<b>Census Tract or BNA</b>	<b>Consumer Loans</b>		<b>Residential Real Estate Loans</b>		<b>Small Farm</b>	
	Number	Amount	Number	Amount	Number	Amount
201	76%	69%	77%	65%	73%	93%
202	4%	8%	8%	10%	2%	1%
9703	10%	15%	8%	13%	11%	3%
9704	4%	4%	5%	7%	5%	2%
104	6%	4%	2%	5%	9%	1%
<b>TOTALS</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>

The loan data indicate the bank extends the majority of its consumer, residential real estate, and small farm loans in census tract 201, which is the location of the bank and the city of Alcester. Each geography's median family income as a percentage of the relevant statewide nonmetropolitan or MSA median family income varies between 86.5% and 116.5%. The two geographies with the lowest relative median family income percentages are MSA census tract 104 and BNA 9704. However, as noted previously, tract 201 has the lowest median family income of the geographies. As the data show, the bank extends loans to

people and farms in these areas; however, its activity in tract 104 and BNA 9704 is less than expected given the assessment area's demographics. Approximately 16% of the assessment area's population resides in MSA census tract 104 while approximately 24% resides in BNA 9704. It appears that the bank's loan activity in these areas is a function of proximity. Other financial institutions are located between these geographies and the bank. The concentration of the bank's lending in census tract 201 is reasonable given the bank's relatively small size and location relative to other institutions.

The bank's loan penetration throughout the assessment area is reasonable given the bank's size as well as the assessment area's size and demographics. Therefore, the bank meets the standards for satisfactory performance in this category

#### GENERAL

The evaluation did not reveal any violations of the substantive provisions of the fair housing and fair lending laws and regulations. The bank has not received any CRA complaints since its last evaluation.

