

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 The State Bank of Townsend, Townsend, Montana, prepared by the Federal Reserve Bank of Minneapolis, the institution's supervisory agency, as of January 27, 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 "Outstanding."

Several factors support the bank's outstanding rating. First, the bank maintains a high loan-to-deposit ratio. Second, it has made a significant number of loans within its assessment area and exceeds the standards for satisfactory performance in this category. Third, based on an analysis of the bank's loans, the bank's record of lending to borrowers of different income levels and to small businesses and farms is exceptional and materially exceeds the standards for satisfactory performance. The bank's strong penetration of real estate lending to moderate-income borrowers is particularly noteworthy. Finally, the bank has engaged in meaningful services to promote access to credit. These services enhance the overall CRA performance.

The following table indicates the performance level of The State Bank of Townsend, Townsend, Montana, with respect to each of the five performance criteria.

SMALL INSTITUTION ASSESSMENT CRITERIA	THE STATE BANK OF TOWNSEND TOWNSEND, MONTANA 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 Income Levels and to Businesses of Different Sizes	X		
Geographic Distribution of Loans	Analysis was not meaningful.		
Response to Complaints	No CRA complaints were received since the previous evaluation.		

DESCRIPTION OF INSTITUTION

Based on its size and financial condition, the bank is able to meet the credit needs of its assessment area effectively. This is the bank's first evaluation using CRA evaluation procedures adopted in November 1995. The bank received an outstanding rating at its last CRA evaluation, which used the previous CRA evaluation procedures. The bank operates a full-service office in Townsend, Montana, plus automated teller machines at the bank and in Three Forks and East Helena, Montana.

The bank's size supports its ability to meet credit needs in its assessment area. According to the December 31, 1996, Report of Condition ("ROC"), the bank had total assets of approximately \$22.7 million. Since December 31, 1995, the bank's net loans and deposits have increased by approximately \$1.9 million and \$1 million, respectively. The bank's loan portfolio is composed of approximately 59% commercial/agriculture, 28% real estate, 13% consumer, and .3% other loans. This loan mix has remained relatively stable since the last evaluation. The composition of the bank's loan portfolio reflects the demand for specific types of loans by residents of the assessment area.

The bank offers a variety of loan products to meet the credit needs of residents, businesses, and small farms within its assessment area. It extends open- and closed-end consumer, residential real estate, agriculture, and commercial loans. Beyond offering these conventional loan products, the bank participates in several government loan and grant programs, including the Small Business Administration and Farm Services Agency loan programs, Montana Board of Housing programs, and Cash Assistance First-Time Home Buyers program.

DESCRIPTION OF THE STATE BANK OF TOWNSEND'S ASSESSMENT AREA

The bank's assessment area is defined as Broadwater County, Montana. Located in west-central Montana, the county comprises block numbering areas ("BNAs") 9832 and 9833. Both BNAs are designated middle income. According to 1990 census figures, Broadwater County has a population of 3,318. Townsend is the county seat for Broadwater County and the largest community in the assessment area; according to 1990 census data, it has a population of 1,635. Located roughly 30 miles southwest of Helena, Broadwater County occupies a broad river valley that includes the Canyon Ferry Reservoir and Missouri River and is surrounded by mountain ranges.

According to a member of the community contacted during the evaluation as well as information obtained from bank management, the county's major industries are agriculture, forestry, mining, and tourism. The banking environment is somewhat competitive. In addition to the subject bank, there is a savings bank in Townsend and several financial institutions in Helena, including branch offices of large regional banking organizations.

CRA divides income levels into four categories: low, moderate, middle, and upper. Because the bank's assessment area is not in a metropolitan statistical area, the categorization of a borrower or BNA's income is determined relative to the statewide nonmetropolitan median family income. Low-income individuals have incomes of less than 50% of the statewide nonmetropolitan median family income, while moderate-income individuals have incomes of at least 50% but less than 80% of this amount. The regulation defines a middle-income person as one with an income of at least 80% but less than 120% of the statewide nonmetropolitan median family income. An individual with an income that is 120% or more of the statewide nonmetropolitan median family income is considered an upper-income person. BNAs are classified using similar categories based on the level of the median family income in the geography.

As previously mentioned, the BNAs in the bank's assessment area are middle

income. According to 1990 census data, the assessment area's median household income is \$20,274 while the median family income is \$24,180. The median household and median family income figures for nonmetropolitan areas in Montana are \$22,345 and \$27,352, respectively. Of the 1,309 households in the assessment area, approximately 22% are low income, 21% are moderate income, 20% are middle income, and 37% are upper income. Approximately 17% of the households and 13% of the families in the assessment area have incomes below the poverty level.

Examiners contacted a local government representative as part of the bank's CRA evaluation. Examiners used information from this contact as well as information from bank management to help evaluate the bank's CRA performance.

The bank's assessment area consists of a homogeneous population. According to the community contact, Townsend continues to be a retirement community. There has been some migration of families with school-age children to the area in recent years. School enrollment is up approximately 100 students since 1990.

According to the Montana Department of Labor and Industry, the population in Broadwater County increased by approximately 359 between 1990 and 1994. The area's community credit needs have a strong reliance on agriculture, mining, and industry. The overall economy in the bank's assessment area since the last evaluation has been stable, despite volatile cattle prices in Montana and a weaker than average tourist season.

CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA

The bank's performance in meeting the credit needs in its assessment area is outstanding. Much of the analysis on the following pages is based on a statistical sample of 77 consumer, 62 commercial/agricultural loans, and 40 residential real estate loans originated by the bank in the 12 months preceding the evaluation. The criteria detailed below were reviewed to determine this rating.

LOAN-TO-DEPOSIT RATIO ANALYSIS

The bank's loan-to-deposit ratio is high and exceeds the standards for satisfactory performance. Based on quarterly ROC data, the bank's average net loan-to-deposit ratio since the previous evaluation is 74%. If included, secondary market loan sales would increase the bank's quarterly average net loan-to-deposit ratio a few percentage points. The following chart, based on quarterly ROC data since the previous evaluation, shows the bank's net loan-to-deposit ratio has ranged from 67% to 80%. According to bank management, the increases in net loans during the first, second, and third quarters of 1996 were due to normal expansion of small business and agricultural operating demands. The bank also extensively marketed its residential real estate loan products during that time. According to bank management, the increase in deposits during the last three quarters of 1996 were due to aggressive deposit solicitations. The quarter ending December 31, 1996, shows a decrease in net loans that is due to the normal cycle of loan paydowns on business and agricultural credits.

QUARTER ENDING DATE	NET LOANS* (In thousands)	DEPOSITS* (In thousands)	NET LOAN-TO- DEPOSIT RATIO *
December 31, 1996	\$14,954	\$20,353	74%
September 30, 1996	\$15,460	\$19,256	80%
June 30, 1996	\$14,466	\$18,854	77%
March 31, 1996	\$13,181	\$18,913	70%
December 31, 1995	\$13,048	\$19,332	67%

*This quarterly information is provided to illustrate trends only.

According to its September 30, 1996, Uniform Bank Performance Report ("UBPR"), the bank's 80% loan-to-deposit ratio is well above its national peer group average of 63%. The bank's ratio places it in the 89th percentile when compared with its peers. A comparison with local competitors also was made using quarterly ROC data from December 31, 1995, to September 30, 1996. The following chart identifies the asset size and quarterly average net loan-to-deposit ratios for the bank and its local competitors.

BANK	TOTAL ASSETS (September 30, 1996) (In thousands)	QUARTERLY AVERAGE NET LOAN-TO-DEPOSIT RATIO
Subject Bank	\$ 22,057	74%
Competitor A	\$ 104,296	84%
Competitor B	\$ 24,624	69%
Competitor C	\$ 14,929	71%
Competitor D	\$ 13,234	56%

The subject bank's quarterly average net loan-to-deposit ratio compares favorably with the ratios of competitors with similar assets. Only one bank in the chart above has a higher average quarterly loan-to-deposit ratio than the subject bank, and the total assets of the competitor are approximately five times larger than the subject bank's total assets. Two competitors have loan-to-deposit ratios similar to the subject bank's and one competitor's loan-to-deposit ratio is significantly lower than the subject bank's. In addition, the December 31, 1996, UBPR indicates the bank's average net loans to assets was 64.66%. The average for all banks in Montana with assets less than \$25 million is 60.13%. Accordingly, the bank devotes a higher percentage of its assets to loan activity than similar-sized institutions in Montana.

Overall, based on area loan demand, the lack of any identified unmet credit needs, the bank's UBPR peer ranking, local bank competition, and the level of loans relative to similar-sized institutions throughout Montana, the bank's loan-to-deposit ratio is high and exceeds the standards for satisfactory performance.

DISTRIBUTION OF CREDIT WITHIN THE ASSESSMENT AREA

Examiners reviewed a statistical sample of credit extensions originated by the bank in the last 12 months. The review included the bank's three major product lines, commercial/agricultural, residential real estate, and consumer loans. A substantial majority of the bank's loans in the sample are made within the assessment area. The following table shows a high concentration of the bank's lending within the assessment area. Based on this information, the bank's lending within the assessment area exceeds the standards for satisfactory performance.

PERCENTAGE OF LOANS IN THE ASSESSMENT AREA		
Loan Category	Number of Loans	Amount of Loans
Consumer	87	86
Residential Real Estate	90	88
Agriculture/Commercial	87	90

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

The bank's record of lending to individuals of different income levels is exceptional and, as such, materially exceeds the standards for satisfactory performance. The bank has made a concerted effort to offer a variety of

credit products for low- and moderate-income borrowers. The bank provides consumer and residential real estate loans to individuals of all different income categories, as shown in the following table.

DISTRIBUTION OF LOANS IN THE ASSESSMENT AREA BY BORROWER INCOME LEVEL*				
Loan Type	Low Income	Moderate Income	Middle Income	Upper Income
<u>Consumer</u>				
Total Number of Loans	40%	20%	20%	20%
Total Amount of Loans	43%	18%	16%	23%
<u>Residential Real Estate</u>				
Total Number of Loans	8%	34%	36%	22%
Total Amount of Loans	4%	30%	45%	21%
*Income level is determined based on Montana's 1996 nonmetropolitan median family income of \$34,700.				

The data in the table above shows the level of consumer lending to low- and moderate-income borrowers is very high. The bank originated 60% of its consumer loans, both in amount and number of loans, to low- and moderate-income individuals. Given the generally small size of loans to lower-income borrowers, the high penetration by dollar amount is particularly noteworthy.

The level of consumer real estate lending to low- and moderate-income borrowers is exceptional. As previously mentioned, approximately 43% of the households in the bank's assessment area are classified as low and moderate income. Although the bank's residential real estate lending (42%) appears to mirror the percentage of low- and moderate-income individuals, approximately 23% of the low- and moderate-income households in the assessment area are classified as low income, and 17% of those households are considered below the poverty level. Based on this economic characteristic, the bank's level of residential real estate lending is significantly above the percentage of such households likely to qualify for residential real estate loans in the assessment area. As mentioned previously, a local government official was contacted as part of the evaluation. According to the contact, housing costs in the assessment area have increased dramatically in the last few years.

Most of the bank's commercial and agricultural borrowers are small businesses and small farms. Of the loans in the sample, 98% were to borrowers with gross annual revenues of \$1 million or less. In addition, 87% of the small farm and small business loans in the sample were for amounts of \$100,000 or less, and 9% were for loans between \$100,000 and \$250,000.

Overall, the bank's emphasis on lending to small businesses and small farms along with its very high percentage of consumer and residential real estate loans to low- and moderate-income borrowers shows a strong commitment to meeting the credit needs of all segments of the community and materially exceeds the standards for satisfactory performance.

GEOGRAPHIC DISTRIBUTION OF LOANS

As previously discussed, the BNAs that make up the bank's assessment area are classified as middle income. There are no low-, moderate-, or upper-income BNAs in the assessment area. Information is not available to determine if the bank's lending by geography is reasonable. Therefore, an analysis of the bank's lending by geographic distribution is not meaningful and this area cannot be rated.

SERVICES

The bank has engaged in a number of services that enhance its CRA performance. These services include positions on the loan review committee of one local community development organization and on the economic development committee of a second organization. Bank management provides technical assistance to other local businesses as well.

While these activities enhance the overall performance, the rating of outstanding is largely attributed to the exceptional distribution of loans to borrowers of different income levels and the high loan-to-deposit ratio.

GENERAL

The evaluation did not reveal any violations of the substantive provisions of the fair lending laws and regulations. In addition, the bank did not receive any CRA complaints since the last evaluation.

PUBLIC DISCLOSURE

January 27, 1997
Date of Evaluation

COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION

The State Bank of Townsend
Name of Depository Institution

093010200000
Identification Number of Institution

Townsend, Montana
Address of Institution

Federal Reserve Bank of Minneapolis
250 Marquette Avenue
Minneapolis, Minnesota 55401-2171

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.