

PUBLIC DISCLOSURE

April 14, 1997

COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION

First Navy Bank
06121241

Pensacola, Florida

Federal Reserve Bank of Atlanta
104 Marietta Street, N.W.
Atlanta, Georgia 30303

NOTE: This evaluation is not, nor should it be construed as, an assessment of the financial condition of this institution. The rating assigned to the 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 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 First Navy Bank prepared by the Federal Reserve Bank of Atlanta, the institution's supervisory agency, as of April 14, 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.

Since the bank has received no complaints regarding its CRA performance, and the entire United States is considered its assessment area, it was rated in only two of the five performance categories. Because of the uneven distribution of loans to borrowers of different income levels, and the steady decline in the bank's loan-to-deposit ratio for the past four years, it was rated marginally satisfactory in both categories.

DESCRIPTION OF INSTITUTION

First Navy Bank operates a full-service banking facility on the Naval Air Station (NAS) Pensacola, Pensacola, Florida, and a check-cashing facility at NAS Whiting Field, Milton, Florida. NAS Whiting Field is 30 miles north of Pensacola. The bank is a wholly owned subsidiary of Five Flags Banks, Inc., a bank holding company in Pensacola, Florida. Affiliates of the bank include the parent holding company, Five Flags Banks, Inc.; The Warrington Bank; Bank of the South; and Bank Data, Inc. Total assets reported in the December 31, 1996 Consolidated Reports of Condition and Income (Call Report) were \$45.6 million. No legal or financial impediments exist that would prevent the bank from meeting the credit needs of the military community that it serves.

The bank's customer base consists mostly of military personnel. Generally, the bank offers only three credit products: personal lines of credit, credit cards, and installment loans. The composition of the loan portfolio according to the December 31, 1996 Call Report is as follows:

LOAN TYPE	PERCENTAGE
Loans to individuals:	
Credit cards and related plans	28
Installment	72
Total	100

Because of the transient nature of base personnel and because base personnel have housing provided by the military, home loans and other conventional credit products are not considered primary credit needs.

DESCRIPTION OF ASSESSMENT AREA

First Navy Bank defines its assessment area as NAS Pensacola, Pensacola, Florida; NAS Whiting Field, Milton, Florida; and military personnel and their dependents residing on bases, ships, or installations throughout the world.

Pensacola, the seat of Escambia County, is located in northwest Florida on the Florida Panhandle. The city is strategically positioned along the Gulf Intracoastal Waterway. NAS Pensacola, located 10 minutes west of downtown Pensacola, serves as the launching point for the flight training of every naval aviator, naval flight officer, and enlisted air crewman. The candidates attending training are from all over the United States.

Data compiled by the NAS Pensacola Public Affairs Office shows base population of 15,630 for the quarter ended December 31, 1996. The population is distributed as follows: enlisted students - 5,239; officer students - 2,266; enlisted staff - 2,830; officer staff - 857; and civilian employees (both appropriated and nonappropriated) - 4,438. Because NAS Pensacola is a training facility, the average length of time a person is stationed on the base is as follows: newly commissioned officer candidates - 16 weeks; enlisted military students - 3 to 4 months; and permanent officers or enlisted staff - 3 to 4 years.

CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA

Loan-to-Deposit Ratio Analysis

First Navy Bank's average loan-to-deposit ratio for the five quarters since the previous examination is 15.8 percent. Both total loans and total deposits have declined since the last examination, but a 4 percent decline in loans and only a 1 percent decline in deposits resulted in an overall decrease in the loan-to-deposit ratio from 16.4 percent as of the last examination to 15.9 percent on December 31, 1996. Several factors contribute to the low ratio, including the bank's focus on small dollar consumer loans. Of the 114 lines of credit extended during the six-month period ended February 1997, 111 (97 percent) were for amounts of \$2,000 or less. Of the 175 automobile loans made during the same time period, 91 (52 percent) were for amounts of \$10,000 or less.

The 289 loans made during this period are indicative of weak loan demand caused in part by cutbacks

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in military spending which impacted civilian base personnel and the number of potential military loan applicants passing through the installation. However, the recent assignment of 5,000 military personnel to the base from NAS Memphis Station should have a positive effect on loan demand and help to improve the banks loan-to-deposit ratio.

CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA (CONTINUED)

Loan-to-Deposit Ratio Analysis (Continued)

Two additional factors negatively affect the bank's loan-to-deposit ratio. On the 15th and last day of each month, First Navy Bank has a large volume of military and retirement pay directly deposited into demand accounts. These funds are generally drawn down rapidly, but cause a 3 percent drop in the bank's loan-to-deposit ratio on the last day of each month. Second, the bank has three large commercial depositors who maintain approximately \$5 million in accounts with the bank. These customers do not have loan relationships with the bank, and the funds may be withdrawn at any time; however, the funds cause the bank's loan-to-deposit ratio to be about 3 percent lower than it would be otherwise.

Competitive factors have also contributed to the low loan-to-deposit ratio. A federal credit union is located on the base, and another credit union is located just outside of the facility. Other major competitors include banks finance companies and pawn shops located off-base and used car dealers offering longer terms and 100 percent financing (the bank offers only 36- and 48-month financing).

Given the bank's focus on small dollar consumer loans, low loan demand, and strong competitive factors, the 15.8 percent average loan-to-deposit ratio since the previous examination is considered reasonable.

Lending in Assessment Area

According to Regulation BB, section 228.41(f), a bank whose business predominantly consists of serving the needs of military personnel or their dependents who are not located within a defined geographic area may delineate its entire deposit-customer base as its assessment area. The bank serves a military community of depositors consisting of active duty and retired military personnel and their dependents. Customers may reside at various locations throughout the United States or at United States military bases overseas. According to the regulation, the United States can be considered as the bank's assessment area. Therefore, the bank's record of lending in its assessment area was not evaluated.

CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA (CONTINUED)

Lending to Borrowers of Different Income Levels

First Navy Bank's performance with regard to lending to borrowers of different income levels is marginally satisfactory. Because the bank's customer base consists principally of military personnel who are not located within a defined geographic area, it was necessary to define its community to include the entire deposit base without regard to geographic proximity to the military base. Since the customer base was not confined to a particular region, demographic information concerning their income levels was unavailable. Therefore, a universe of potential borrowers was defined. The universe included all of the 485 approved and denied applications that were received from throughout the United States between September 1996 and February 1997. Information from this universe was used to figure a median annual income (\$27,060) and to determine the percentage of applicants that are considered low-, moderate-, middle-, and upper-income. The chart below depicts the income ranges of the four categories and the percentage of the universe that falls within each income category.

INCOME CATEGORY	INCOME RANGE	% OF UNIVERSE
Low-income (<50 percent of the median income)	\$1 to \$13,530	24.7
Moderate-income (between 50 and 80 percent of the median income)	\$13,531 to \$21,648	19.6
Middle-income (between 80 and 120 percent of the median income)	\$21,649 to \$32,472	11.8
Upper-income (over 120 percent of the median income)	\$32,473 and above	43.9

Automobile loans and small lines of credit are the primary loan products. A sample of 175 automobile loans and 114 lines of credit was analyzed to assess the bank's performance with regard to lending to borrowers of different income levels. The distribution of the 289 approved loans was compared to the income distributions in the chart above. The chart below illustrates an uneven distribution among the

income levels of those seeking automobile loans, but an income distribution among those applying for revolving loans that more closely matches their representation in the universe.

CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA (CONTINUED)

Lending to Borrowers of Different Income Levels (Continued)

BORROWER INCOME LEVEL	AUTOMOBILE LOANS		REVOLVING LOANS	
	NUMBER	PERCENT	NUMBER	PERCENT
Low	5	2.9	16	14.0
Moderate	6	3.4	25	21.9
Middle	15	8.6	23	20.2
Upper	149	85.1	50	43.9
Total	175	100.0	114	100.0

The bank has been most successful in extending automobile loans to upper-income borrowers. As noted above, upper-income applicants constituted 43.9 percent of the applicants, but received 85.1 percent of the automobile loans. Alternatively, low-income applicants, who made up 24.7 percent of the applicants, received only 2.9 percent of the automobile loans. Penetration of moderate-income applicants was slightly better; they received 3.4 percent of the loans while constituting 19.6 percent of the applicants. Middle-income borrowers were the only group that received automobile loans at a rate close to their representation in the loan universe.

The bank promotes its loan products primarily through statement stuffers and accepts a significant volume of loan applications by means of a toll-free telephone number. Bank management indicated that most of the loans are to the high income category because a vast majority of the applicants for automobile loans are the more highly paid officers. They indicated that lower paid enlisted personnel would have problems qualifying for automobile loans. According to President Woodbury, these circumstances are caused primarily by two factors. One, most service personnel establish banking relationships at their initial base post; because more officer candidates=initial assignments are on the Pensacola base, more return as long-term customers. Second, the requirement that a borrower establish a deposit relationship, deposit his entire paycheck or an allotment of \$1,000 or more per month, and have previous credit experience limits access to credit by lower paid personnel. Based on characteristics of applicants in the universe, those

applying for automobile loans are generally in the upper income category. The median income of those applying for automobile loans (\$48,000) was considerably higher than the median for the universe (\$27,060). Higher paid individuals comprise the majority of the applicants (67 percent) compared to only 15 percent from the low income category.

CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA (CONTINUED)

Lending to Borrowers of Different Income Levels (Continued)

Of greater concern, is the significantly higher rejection rate for low-income applicants (86 percent) in comparison to the rejection rate for upper income applicants (only 5 percent). The large differential may be attributed to several factors including the bank's lending guidelines. The bank offers very competitive interest rates, but does not extend automobile loans for a term greater than four years. The shorter term places a greater burden on those in the low income category and may encourage them to seek alternate financing.

While most of the denials (approximately 72 percent) were attributed to derogatory credit, low income applicants were not affected in a disproportionate manner. However, the second most common reason for denial was **Insufficient or Limited Credit Experience** which affected approximately 26 percent of the denied enlisted personnel. This policy is especially restrictive given the bank's requirement that customers 1) open a checking account as a condition of obtaining a loan; 2) authorize the bank to automatically deduct loan payments by virtue of an addendum to the note; and 3) increase the note rate by 5 percent if the direct deposit is discontinued.

The distribution of small revolving loans was considerably better. The percentage of revolving loans to upper-income applicants was an exact reflection of the upper-income representation in the loan universe. Lending in middle- and moderate-income categories was also close to those applicants' representation in the loan universe. Whereas low-income applicants represented 24.7 percent of the universe, they received only 14 percent of the loans; however, this is considered reasonable because some of the incomes were too low to service any debt.

Information on the **Economic Impact** of the U.S. Navy in the Pensacola area was also provided by bank management. The report did not include individual income information nor define the composition of **Economic Impact**, therefore, it was inappropriate to calculate the median income from this source. However, the report contained sufficient data to compute the average economic impact of students (both officers and enlisted) and permanent duty personnel (officers, enlisted personnel, and civilians) who were physically located on the base as of December 31, 1996. That information is illustrated in the chart below.

CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA
(CONTINUED)

Lending to Borrowers of Different Income Levels (Continued)

PERSONNEL	AVERAGE ECONOMIC IMPACT	% OF POPULATION
Officers (Staff)	\$19,649	7.1
Officers (Students)	\$12,473	13.4
Enlisted (Staff)	\$10,183	22.5
Enlisted (Students)	\$6,349	29.7
Civilians	\$8,262	27.3

Based on the economic impact information, the income levels of individuals in the loan sample were considerably higher than the incomes of those either stationed or in training on the Pensacola base. One of the explanations given for the lack of automobile applications from those other than officers was that the income of the lower ranking enlisted personnel would only support the \$300 to \$500 signature loans.

However, the \$15,600 median income for the rejected loan applicants contained in the sample was considerably higher than the \$6,349 annual economic impact of lower ranking enlisted personnel located on the base. This is an indication that most of the applications contained in the universe were not from base personnel.

Geographic Distribution

Because the bank's assessment area is the entire United States, a geographic analysis of the bank's loan portfolio is of little benefit in analyzing the bank's lending practices, and this performance criterion was not evaluated.

Complaints

No complaints relating to CRA have been filed since the previous examination.

Compliance with Antidiscrimination Laws

The bank is in compliance with the substantive provisions of the antidiscrimination laws and regulations.

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No evidence of discrimination or the use of illegal credit practices was noted during the review of bank policies and procedures. No practices have the intent or the effect of discouraging applicants.