

## 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 Farmers State Bank of Denton, Denton, Montana, prepared by the Federal Reserve Bank of Minneapolis, the institution’s supervisory agency, as of July 28, 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.”

There are several factors to support the bank’s outstanding rating. First, the bank has maintained a high loan-to-deposit ratio since the last evaluation. Second, based on analysis of the loans, the bank lends to borrowers of many different income levels and to small businesses and farms. Third, the bank’s efforts in community development lending are significant. Fourth, the bank engages in a number of community development services that enhance its CRA rating. Finally, the bank has made a significant majority of its loans within its assessment area.

## **DESCRIPTION OF INSTITUTION**

Based on its size and financial condition, the bank is able to meet the credit needs of the communities in its assessment area effectively. The bank received an outstanding rating at its last CRA evaluation in August 1995. According to the June 30, 1997, Report of Condition (“ROC”), its total assets are approximately \$13.5 million. Since September 30, 1995, the bank’s loans and deposits have remained relatively stable with increases of \$1.1 million and \$.7 million, respectively, while total assets have increased by \$1.6 million. A significant portion of the bank’s loan portfolio includes agriculture-related loans, which mirrors the agricultural nature of the local economy. According to the June 30, 1997, ROC, agricultural loans comprise 72% of the bank’s portfolio. The remainder of the portfolio includes 13% commercial, 13% consumer, and 2% other loans.

Management stated that the bank does not offer consumer real estate loans because of lack of demand and the significant cost to retain a qualified loan officer for that purpose. The bank currently refers all real estate loan applicants to the four banks operating in Lewistown, Montana. The evaluation did not reveal any evidence of unmet demand for real estate loans.

The bank operates a full-service office in Denton. The bank offers many types of loan products that serve local residents’ credit needs. Its agricultural loan products include farm and ranch lines of credit, operating loans, term loans, and real estate mortgage loans. To supplement its conventional agricultural loan programs, the bank offers Farm Service Agency-guaranteed and -subordinated loans. The bank is also certified to offer Small Business Administration (“SBA”) loans although it has not been actively making SBA loans for some time. The bank’s low level of involvement in the SBA program reflects the community’s lack of demand for this type of loan. Commercial customers may obtain conventional operating loans and inventory financing. In addition to its agricultural and commercial products, the bank provides a variety of consumer loan products. The bank’s products appear appropriate for its community’s credit needs.

## **DESCRIPTION OF FARMERS STATE BANK OF DENTON’S ASSESSMENT AREA**

The bank defines its assessment area as all of Judith Basin and Fergus counties in central Montana. The assessment area contains block number areas (“BNA”) 9708, 9709, and 9710 in Judith Basin County and BNAs 9696, 9697, 9698, 9699, 9701, 9702, and 9703 in Fergus County. All of the BNAs are designated middle income. The bank is located in BNA 9697 in western Fergus County. Denton is a small, rural community with a population of approximately 350, according to 1990 census data. Denton is located in a remote and sparsely populated region of central Montana about 100 miles east of Great Falls, Montana, and 40 miles northwest of Lewistown.

According to the 1990 census figures, the bank’s assessment area has a total population of 14,365. Judith Basin County is sparsely populated with an approximate population of 2,282. Fergus County has a population of 12,083, of which over 60% reside in Lewistown, the county seat. All other communities in the assessment area, including Stanford, Hobson, Moore, Winifred and Grass Range, have considerably smaller populations.

The largest employers in the assessment area provide health, government, and educational services. The U.S. Bureau of Land Management has its district office in Lewistown. Lewistown is also the site of the Central Montana Medical Center, which owns a nonprofit, full-service hospital that provides medical

services to a large area of central Montana. Lewistown also has a mental health center and four nursing homes. The concentration of available health care facilities provide services for and meet the needs of the population over the age of 65, which comprise approximately 20% of the assessment area's population.

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 that comprise the bank's assessment area are middle income. As a percentage of statewide nonmetropolitan median family income, these BNAs range from 81.8% to 108%. According to the 1990 census data, the assessment area's median household income is \$21,584 while the median family income is \$25,929. As a comparison, the median household and median family income figures for nonmetropolitan areas in Montana are \$22,345 and \$27,352, respectively. Of the 5,551 households in the assessment area, approximately 22% are low income, 17% are moderate income, 22% are middle income, and 39% are upper income. Approximately 14% of the households and 11% of the families have incomes below the poverty level.

Examiners contacted an individual familiar with the agricultural credit needs in the assessment area as part of the bank's CRA evaluation. Information obtained from this individual along with information received from bank management was used in evaluating the bank's CRA performance.

According to the community contact as well as information obtained from bank management, the assessment area's major industry is agriculture. Small grain farming and cattle ranching are the region's primary agricultural activities. Small grains consist of winter wheat, barley, and hay. Currently, the agricultural economy is stable and growing slightly and unemployment is low. The last several years have produced low cattle prices, which has affected the income of the area's ranchers. Both bank management and the community contact indicate there is guarded optimism concerning this year's cattle and crop prices. The community contact stated that the agricultural cash receipts for Fergus County are estimated to run approximately \$58 million to \$60 million this year. This is only a slight increase from the cash receipts reported in the Montana Agricultural Statistics for 1994. Although the current year looks positive for cattle ranchers, the community contact and bank management indicated it will take two to three years to even out the losses caused by severe winters and low prices.

The community contact indicated that the tourism trade is supported by several local festivals and renewed interest in the area's ghost towns. Although tourism continues to grow in the area around Lewistown, which has encouraged community development and restoration projects, there is little opportunity for community development in the rest of the assessment area because of the sparse population.

The banking environment is competitive. Although the subject bank is the only financial institution in Denton, there are several banks, a savings and loan, and a credit union in Lewistown, including a branch office of a large regional banking organization.

## CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA

Based on its size, the bank has done an outstanding job of meeting the credit needs of its assessment area. Much of the analysis on the following pages was based on a statistical sample of 99 agricultural loans and 50 consumer loans the bank originated in the 12 months preceding the evaluation. The criteria discussed below were reviewed in determining this rating. In assigning the overall rating, greatest weight was placed on the loan-to-deposit ratio and assessment of lending to borrowers of different income levels and businesses and farms of different sizes. These two factors along with the bank's community development lending most closely measure the bank's efforts to meet the credit needs of all segments of its community.

### LOAN-TO-DEPOSIT RATIO ANALYSIS

The bank's loan-to-deposit ratio significantly exceeds the standards for satisfactory performance based on the ratio's consistently strong level, loan demand, and lack of any unmet credit needs. Since the previous evaluation, the quarterly average of the bank's net loan-to-deposit ratio is 84.9%. According to the June 30, 1997, ROC, the bank's net loan-to-deposit ratio was 94.2%. The following chart, based on quarterly ROC data, shows the consistently high loan activity for the bank since the previous evaluation.

DATE	NET LOANS (IN THOUSANDS)	DEPOSITS (IN THOUSANDS)	NET LOAN-TO-DEPOSIT RATIO
June 30, 1997	\$9,798	\$10,397	94.2%
March 31, 1997	\$8,982	\$10,842	82.8%
December 31, 1996	\$9,220	\$11,557	79.8%
September 30, 1996	\$9,371	\$11,509	81.4%
June 30, 1996	\$10,333	\$10,981	94.1%
March 31, 1996	\$8,402	\$11,050	76.0%
December 31, 1995	\$8,219	\$10,030	81.9%
September 30, 1995	\$8,657	\$9,651	89.7%

The fluctuations in loan volume reflect the cyclical nature of an agricultural based economy. For example, as shown in the above table, the lower loan volume in the first quarter of 1996 is a reflection of agricultural loan paydowns, and an increase in grain prices and volume, in addition to an increase in core deposits.

According to its March 31, 1997, Uniform Bank Performance Report ("UBPR"), the bank's 82.8% loan-to-deposit ratio is significantly above its peer group's average loan-to-deposit ratio of 59.89%. The UBPR ranks the bank in the 95th percentile of its peer group. The high loan-to-deposit ratio as of June 30, 1997, is because seasonal agricultural loan line advances are at their peak and the bank continues its commitment to extend credit to local business operations. These numbers do not reflect all of the bank's lending in the community because the bank has sold loan participations in order to accommodate its agricultural customers' credit needs.

The bank's nearest agricultural lending competitors are Basin State Bank in Stanford, Montana (30 miles southwest of Denton), and the Norwest Bank Montana, National Association, Billings, Montana, branch in Lewistown (approximately 40 miles southeast of Denton). Because both banks have substantially more assets than the subject bank, a loan-to-deposit comparison is not warranted. However, the March 31, 1997, UBPR indicates the bank's average net loans to assets is 61%. This average mirrors the average net

loans to assets for all banks in Montana with assets less than \$25 million. Accordingly, the bank devotes a similar percentage of its assets to loan activity as similar-sized institutions in Montana.

In addition to the high loan-to-deposit ratio, the bank is currently financing the construction of a new automated plant and storage facility for a local agricultural-based distribution business. This community development loan is 90% guaranteed by Rural Business Coop Services. It is projected that the company will employ seven or eight people as it reaches capacity, making it one of the largest employers in the Denton community. Jobs created by the plant will generally be provided to low- and moderate-income people.

The bank has flexible lending standards and participates in loans within the community that are vital to maintaining its economic life and stability. Bank management believes losing any business on the main street of Denton would negatively affect the other few businesses and be devastating to the local economy. Accordingly, the bank actively supports these enterprises with flexible loan criteria.

Overall, based on area loan demand, the bank's consistently strong loan-to-deposit ratio, its UBPR ranking, its commitment to community development lending, and the lack of any identified unmet credit needs, the bank's loan-to-deposit ratio significantly exceeds the standard for a satisfactory performance.

**COMPARISON OF CREDIT EXTENDED INSIDE AND OUTSIDE THE ASSESSMENT AREA**

A review of the statistical sample of the loans originated by the bank since the last evaluation reveals that a significant majority of the loans were made inside the assessment area. Accordingly, the bank exceeds the standards for satisfactory performance in this area. The following table shows the percentage of loans within the assessment area based on total number and loan amount in each major loan category.

<b>DISTRIBUTION OF LOANS IN AND OUT OF THE ASSESSMENT AREA</b>								
<b>Loan Type</b>	<b>Inside</b>				<b>Outside</b>			
	Number of Loans	%	Amount of Loans (In thousands)	%	Number of Loans	%	Amount of Loans (In thousands)	%
Consumer (50)	40	80	441	89	10	20	56	11
Small Farm (99)	92	93	2,863	93	7	7	223	7
<b>Total (149)</b>	<b>132</b>	<b>89</b>	<b>3,304</b>	<b>92</b>	<b>17</b>	<b>11</b>	<b>279</b>	<b>8</b>

As the table shows, a substantial majority of the bank's loans in the sample were made within the bank's assessment area. Based on the high concentration of lending within the assessment area, particularly the concentration of small farm loans, the bank exceeds the standards for satisfactory performance in this category. As discussed previously, approximately 85% of the bank's loan portfolio is agricultural and commercial loans.

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

The bank's level of lending to individuals of different income levels significantly exceeds the standards for satisfactory performance. The following table shows the percentage of consumer 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 Borrowers</b>	<b>Moderate-Income Borrowers</b>	<b>Middle-Income Borrowers</b>	<b>Upper-Income Borrowers</b>
<b>Consumer</b>				
Total Number of Loans	38%	35%	22%	5%
Total Amount of Loans	11%	28%	14%	46%
*Income level based on Montana's 1997 non-metropolitan statistical area median family income of \$36,100.				

The data in the table indicate that the bank originated a substantial majority, 73%, of its consumer loans to low- and moderate-income borrowers. Although the loan volume is only 39% in this category, the total number of loans to low- and moderate-income borrowers shows the bank's willingness to lend small-dollar loans to these borrowers. This is significant because agricultural economic conditions in the past few years have had a negative impact on the annual income of the average borrower in the assessment area. The reduced income of the ranchers affects all related agricultural based businesses. As mentioned in the Description of Assessment Area section, approximately 40% of the households in the assessment area are classified as low and moderate income according to the 1990 census figures. The bank's level of lending to low- and moderate-income borrowers significantly exceeds the demographic distribution. Although the bank does not provide a consumer real estate product, it assists those customers interested in real estate by referring them to and working closely with the financial institutions in Lewistown during the loan process.

Small farm operating loans make up approximately 69% of the bank's loan portfolio. The definition of small business or small farm is a business or farm with gross annual revenues of \$1 million or less. Of the loans in the sample, 100% of the agricultural loans fit into this category. Approximately 90% of the agricultural loans in the sample were for loan amounts of \$100,000 or less. This distribution is consistent with the bank's asset size and the bank's overall assessment area economic conditions.

The bank's emphasis on consumer lending to low- and moderate-income borrowers along with its high percentage of loans to small farms shows a strong commitment to meeting the credit needs of the entire community. The bank's performance in this category significantly 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. As previously mentioned, as a percentage of statewide nonmetropolitan median family income, these BNAs range from 81.8% to 108%. Bank management indicated the low-, moderate-, and upper-income residents are not concentrated in any particular area but are dispersed throughout the assessment

area. Approximately 45% of the bank's consumer and small farms loans are concentrated in the BNA where the bank is located. Another 18% of the bank's loans are located in the two BNAs that include Lewistown, the largest population center in the assessment area. The bank does not have any loans in BNA 9708, which is very sparsely populated and located quite a distance from the bank and closer to other financial institutions. All other consumer and small farm loans are evenly dispersed throughout the remaining BNAs.

### SERVICES

The bank's loan officers provide technical financial assistance to several commercial and agricultural businesses. This assistance includes creating and incorporating viable accounting systems, providing financial review of business records and making appropriate recommendations, and giving assistance in applying for government-insured loans. Many of these businesses employ low- and moderate-income people.

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

### GENERAL

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

## **PUBLIC DISCLOSURE**

July 28, 1997

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Date of Evaluation

## **COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION**

Farmers State Bank of Denton

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Name of Depository Institution

093003200000

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Identification Number of Institution

Denton, Montana

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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.