

PUBLIC DISCLOSURE

January 13, 1997

COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION

Farmers and Merchants Bank

05512870

P. O. Box F

Timberville, Virginia 22853

Federal Reserve Bank of Richmond

P. O. Box 27622

Richmond, Virginia 23261

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 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 Farmers and Merchants Bank, Timberville, Virginia, prepared by The Federal Reserve Bank of Richmond, the institution's supervisory agency, as of January 13, 1996. The agency rates the CRA performance of an institution consistent with the provisions set forth in Appendix A of 12 CFR Part 228.

INSTITUTION'S CRA RATING: This institution is rated Outstanding.

The bank's loan-to-deposit ratio is considered more than reasonable given its financial capacity, location, and demand for credit in the area. A majority of loans sampled during the examination were provided to residents of the assessment area. Furthermore, the institution's high level of lending to low- and moderate-income borrowers demonstrates an outstanding performance. While there are no low- or moderate-income census tracts within the assessment area, 98% of the sampled loans were extended to persons residing in middle-income tracts. This loan distribution compares favorably to the 52% of borrowers residing in such areas. Investments and services were also considered in the bank's CRA performance rating. The institution has invested in two statewide Housing Equity Funds. These funds are used to finance low- and moderate-income housing throughout the Commonwealth of Virginia.

The following table indicates the performance level of Farmers and Merchants Bank with respect to each of the five performance criteria.

SMALL INSTITUTION ASSESSMENT CRITERIA	<u>Farmers and Merchants Bank</u> 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 Incomes and to Businesses of Different Sizes	X		
Geographic Distribution of Loans	X		
Response to Complaints	No complaints have been received since the prior examination.		

DESCRIPTION OF INSTITUTION

Farmers and Merchants Bank operates five offices located in Timberville (main office), Bridgewater (1), Broadway (1), and Elkton (2), Virginia. As of September 30, 1996, the bank had \$152 million in assets, of which 71% were loans. Various deposit and loan products are available through the institution including loans for home purchase, residential construction, home improvement, consumer, and commercial purposes. The loan portfolio as of September 30, 1996, was comprised of the following: 81% real estate secured (consumer and business), 14% consumer, and 5% commercial. Based on the number of loans extended during the previous six months, consumer purpose loans were identified as the primary credit product offered by the bank. The institution's previous CRA rating was satisfactory.

DESCRIPTION OF ASSESSMENT AREA

The bank's assessment area encompasses all of Rockingham County, Virginia, as well as census tract 702.00 in Augusta County and census tract 408.00 in Shenandoah County. This community is located in the northwestern region of the Commonwealth and is part of Virginia's Shenandoah Valley. The local market is primarily rural and has a population of 64,467, with 71% of the residents living in owner-occupied dwellings. The assessment area consists of 21 census tracts, of which 11 are middle-income and ten are upper-income. There are no low- or moderate-income geographies within the bank's market area.

Industry in the area is dominated by agriculture, principally relating to poultry production. Other business and employment opportunities are provided through small manufacturing operations, government and educational facilities, and tourism. The unemployment rates for Augusta, Rockingham, and Shenandoah Counties are 3%, 2.2%, and 3.9%, respectively, and compare favorably to Virginia's jobless rate of 3.8%. Housing prices continue to be relatively high because of the close proximity to Washington, D. C., and the scarcity of land due to the mountainous terrain. The 1996 nonmetro-politan median family income for Virginia was \$33,600.

A community contact was performed during the evaluation with a private individual knowledgeable about the community to further assist in evaluating the bank's CRA performance. The contact indicated there is a shortage of adequate housing and services for rural, low-income residents in the community.

CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA

LOAN-TO-DEPOSIT RATIO

The institutions's average loan-to-deposit ratio for the previous five quarters is 86% and is considered highly responsive to area loan demand. Considering the institution's financial capacity, size, and current local economic conditions, this ratio exceeds expectations for satisfactory performance. The average loan-to-deposit ratio for banks headquartered in nonmetropolitan areas of Virginia and of similar asset size to Farmers and Merchants Bank is 72%.

LENDING IN ASSESSMENT AREA

To determine the institution's volume of lending within the assessment area, a sample of consumer loans extended during the previous six months was reviewed. This sample consisted of 107 secured and unsecured nonreal estate consumer loans. The distribution is represented in the chart below.

Comparison of Credit Extended Inside and Outside of Assessment Area

	Inside Assessment Area	Outside Assessment Area	Total
Total Number of Loans	85	22	107
Percentage of Total Loans	79%	21%	100%
Total Amount of Loans (000's)	\$464	\$178	\$642
Percentage of Total Amount	72%	28%	100%

As illustrated above, a majority of the number and dollar amounts of the sampled loans have been provided to borrowers residing within the assessment area.

LENDING TO BORROWERS OF DIFFERENT INCOMES AND TO BUSINESSES OF DIFFERENT SIZES

A review of the 85 sampled loans within the assessment area was conducted to analyze borrower income characteristics. The following chart illustrates the distribution of consumer loans extended in the assessment area by borrower income level.

Distribution of Loans by Income Level of Borrower

	Low-Income	Moderate-Income	Middle-Income	Upper-Income	Total
Total Number of Loans	21	36	17	11	85
Percentage of Total Loans	25%	42%	20%	13%	100%
Total Amount of Loans (000's)	\$73	\$179	\$140	\$72	\$464
Percentage of Total Amount	16%	39%	30%	15%	100%

As a means of comparison, the chart below depicts the families residing within the assessment area by low-, moderate-, middle-, and upper-income levels.

Percentage of Families in Assessment Area by Income Level

	Low-Income	Moderate-Income	Middle-Income	Upper-Income	Total
Percentage of Families	11%	16%	25%	48%	100%

When compared to the market distribution of families, the bank's volume of lending to low- and moderate-income individuals (67%) significantly exceeded the percentage of such families residing within the assessment area (27%). Moreover, a majority of the dollar amount of loans extended (55%) were to low- and moderate-income borrowers.

GEOGRAPHIC DISTRIBUTION OF LOANS

The review of consumer loan files also included an analysis of lending distribution among middle- and upper-income census tracts within the institution's assessment area. As previously mentioned, there are no low- or moderate-income geographies within the local market. The following chart depicts loan penetration according to income level of census tract.

Distribution of Loans in Assessment Area by Income Level of Census Tract

	Middle-Income	Upper-Income	Total
Total Number of Loans	83	2	85
Percentage of Total Loans	98%	2%	100%
Total Amount of Loans (000's)	\$455	\$9	\$464
Percentage of Total Amount	98%	2%	100%

When compared to market demographics, the institution's lending performance within the assessment area reflects a high level of lending to residents of middle-income census tracts. The bank's penetration in middle-income tracts represented 98% of the sampled loans and significantly exceeded the percentage of individuals residing in middle-income geographies (55%).

INVESTMENTS AND SERVICES

As of January 13, 1996, the institution had paid \$334,188 towards a \$400,000 commitment to the Housing Equity Fund II of Virginia and \$500 towards a recent \$500,000 commitment to the Housing Equity Fund III of Virginia. These funds, which are provided by numerous corporate investors, are used to finance low- and moderate-income housing throughout the Commonwealth of Virginia. Commitments from all the investors totaled \$10.4 million for the Housing Equity Fund II and will total between \$8 and \$10 million for the Housing Equity Fund III. In lieu of payments, the bank receives tax credits for its investments.

COMPLIANCE WITH ANTIDISCRIMINATION LAWS AND REGULATIONS

No credit practices inconsistent with the substantive provisions of the fair housing and fair lending laws and regulations were identified. Technical violations of the Equal Credit Opportunity Act's Regulation B were noted. Adequate policies, procedures, and training programs have been developed to support nondiscrimination in lending and credit activities.