



PUBLIC DISCLOSURE

NOVEMBER 30, 1998

COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION

**HNB Bank, N.A.
Charter Number 12295**

**101 North Main Street
Harlan, Kentucky 40831**

**Office of the Comptroller of the Currency
Evansville Field Office
101 N.W. 1st Street, Suite 207
Evansville, Indiana 47708-0130**

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 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 **HNB Bank, N.A., Harlan, Kentucky** (HNB) prepared by the Office of the Comptroller of the Currency (OCC), the institution's supervisory agency, as of **November 30, 1998**. The agency rates the CRA performance of an institution consistent with the provisions set forth in Appendix A to 12 C.F.R. Part 25.

HNB received a rating of “Satisfactory” at the last CRA examination dated February 20, 1996. This examination covers HNB’s performance from January 1, 1996 to November 30, 1998.

Institution’s CRA Rating: This institution is rated “**Satisfactory**”.

The following are the primary factors supporting HNB’s rating.

- HNB’s loan-to-deposit ratio is reasonable given its size, its financial condition, current economic factors, and assessment area credit needs.
- A majority of HNB’s loans are made within its assessment areas.
- HNB’s distribution of loans to borrowers of different income levels and businesses of different sizes is reasonable.
- HNB’s geographic distribution of residential real estate, small business, and consumer loans is reasonable.

The following table indicates the performance level of HNB with respect to each of the five performance criteria.

Small Institution Assessment Criteria	HNB Bank, N.A. 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 Areas		X	
Lending to Borrowers of Different Incomes and to Businesses of Different Sizes		X	
Geographic Distribution of Loans		X	
Response to Complaints	No complaints were received since the prior examination.		

DESCRIPTION OF INSTITUTION

HNB is a \$184 million bank headquartered in Harlan, Kentucky. It has six offices in Harlan (4) and Estill (2) counties. In September of 1997, HNB was acquired by Area Bancshares Corporation (ABC), a \$2 billion multi-bank holding company headquartered in Owensboro, Kentucky. ABC owns eleven other financial institutions within the state of Kentucky. Prior to September of 1997, HNB was owned by Cardinal Bancshares, Inc., a bank holding company with total assets of less than \$1 billion.

As of September 30, 1998, HNB's loan portfolio was comprised of residential real estate (\$24 million), commercial real estate (\$33 million), commercial (\$9 million), and consumer (\$41 million) loans totaling \$107 million. There are no legal, financial, or other reasons that would impede HNB's ability to meet the credit needs of its assessment areas.

DESCRIPTION OF ASSESSMENT AREAS

HNB has two assessment areas in southeastern Kentucky consisting of Harlan and Estill counties. Harlan County is located approximately twenty miles from the Virginia state line. Harlan County's economy is depressed, stagnant, and plagued by a high unemployment rate of approximately 12%, which is significantly higher than the state of Kentucky's unemployment rate of 6%. Thirty-four percent of families residing in Harlan County live below the poverty level.

Approximately 34% and 8% of Harlan County’s population receive social security or welfare payments, respectively. The major industry is mining, which provides approximately 2,000 jobs, down from 5,000 jobs in 1994 and 1995. Excluding mining related companies, the primary employers are the county school board, manufacturing companies, and the local hospital. Estill County is located approximately fifty miles southeast of Lexington, Kentucky. Estill County’s local economy is fairly stable with an unemployment rate of approximately 4%. According to a community contact, approximately 50% of those employed work outside the county. Major employers are light manufacturing companies, the county school board, and the local hospital.

Tables 2 thru 5 detail pertinent information concerning HNB and demographic data that was used in connection with our review of HNB’s CRA performance. Information in the tables is broken out for each of the bank’s two assessment areas.

Table 2, detailing HNB’s assessment areas, illustrates that Harlan County is the largest of the two assessment areas as measured by population, number of branches, and total deposits.

Table 2 HNB’s Assessment Areas				
Assessment Areas	Population	Number of Branches	Total Deposits as of 6/30/97 (\$Millions)	Deposit Market Share and Ranking¹ by Assessment Area
Harlan County	36,574	4	\$105	Mkt. Share: 40% Ranking: 1st
Estill County	14,614	2	52	Mkt. Share: 43% Ranking: 1st
Total	51,188	6	\$157	

Source: 1990 Census Data - U.S. Bureau of the Census, Federal Deposit Insurance Corporation and Office of Thrift Supervision’s Summary of Deposits Internet Site, and bank provided information

Competition is strong. Six deposit-taking financial institutions have branch offices within HNB’s assessment areas. HNB is the largest financial institution in Harlan and Estill counties based on deposit market share as of June 30, 1997. HNB’s primary competition includes The Bank of Harlan (Harlan County), Home Federal Bank, FSB (Harlan County), and Citizens Guaranty Bank (Estill County). The Bank of Harlan is the only financial institution, other than HNB, that is headquartered in either Harlan or Estill counties.

¹ Deposit market share and ranking data was provided as a tool for assessing the relative size of HNB. It is not a measure of HNB’s CRA performance.

Table 3 reflects the number of low-, moderate-, middle-, and upper-income geographies by income level. The assessment areas are comprised of 16 geographies. According to 1990 census information, 9 (56%) of the geographies are moderate-income, 6 (38%) are middle-income, and 1 (6%) is upper-income. There are no low-income geographies within HNB's assessment areas.

Table 3 Distribution of Geographies by Assessment Area					
Assessment Areas	Number of Geographies				
	Low-Income	Moderate-Income	Middle-Income	Upper-Income	Total
Harlan County	0	8	3	1	12
Estill County	0	1	3	0	4
Total	0	9	6	1	16

Source: 1990 Census Data - U.S. Bureau of the Census

Table 4 depicts the number and percentage of families within HNB's assessment areas based on their income level. HNB's assessment areas have 14,484 families, of which 32% are low-income, 17% are moderate-income, 18% are middle-income, and 33% are upper-income. This information was used to evaluate HNB's lending of residential real estate and consumer loans to borrowers of different income levels. As of 1998, the statewide adjusted non-MSA median family income was \$29,800.

Table 4 Distribution of Families by Income Level				
Assessment Areas	Low-Income	Moderate-Income	Middle-Income	Upper-Income
Harlan County	3,399 33%	1,739 17%	1,797 17%	3,393 33%
Estill County	1,190 28%	783 19%	783 19%	1,400 34%
Total	4,589 32%	2,522 17%	2,580 18%	4,793 33%

Source: 1990 Census Data - U.S. Bureau of the Census

Table 5 provides information on the number and percentage of businesses by geographic income level. There are 869 businesses within HNB’s assessment areas. This information was used to evaluate HNB’s geographic distribution of small business loans.

Table 5 Number and Percentage of Businesses Based Upon Geographic Income Level						
Assessment Areas		Low-Income	Moderate-Income	Middle-Income	Upper-Income	Total
Harlan County		0	377	105	108	590
Estill County		0	27	252	0	279
Total	#	0	404	357	108	869
	%	0%	47%	41%	12%	100%

Source: Dun & Bradstreet, Inc.

Our discussion with community representatives from Harlan and Estill counties revealed the demand for small business loans is low. The small business loan demand that does exist is for loans with original amounts of less than \$25,000. The demand for residential real estate loans is moderate in Harlan County and good in Estill County. In Harlan County, housing needs were identified as single family, owner occupied housing units for middle- and upper-income individuals. Low-income housing needs, such as rent subsidized housing, are being addressed. In Estill County, housing needs were identified as market rate multi-family housing and renovation of older single family dwellings. These community needs were determined by meeting with the mayor of Harlan, Kentucky and a representative of a community economic development agency in Estill, Kentucky.

CONCLUSIONS WITH RESPECT TO PERFORMANCE TESTS

A non-statistical sample of 30 residential real estate, 25 small business, and 30 consumer loans originated in 1998 was used to evaluate HNB’s CRA performance relating to the geographic distribution of loans and the distribution of loans to borrowers of different income levels and businesses of different sizes.

Loan-to-Deposit Ratio

- **The bank’s loan-to-deposit ratio is reasonable.**

The bank’s loan-to-deposit ratio averaged 73% for the period of 1996, 1997, and year-to-date 1998. This percentage is reasonable given depressed economic conditions, low loan demand, and strong competition from other financial institutions.

Lending in Assessment Areas

- **A majority of loans are originated within the bank's assessment areas.**

Fifty-nine percent of loans originated in 1996, 1997, and year-to-date 1998 were made within HNB's assessment areas. Distressed economic conditions and low loan demand has forced management to look outside its assessment areas for lending opportunities.

Lending to Borrowers of Different Incomes and to Businesses of Different Sizes

- **The bank's distribution of credit reflects a reasonable penetration among individuals of different income levels and businesses of different sizes.**

Residential Real Estate Loans

Table 6 compares HNB's residential real estate lending to borrowers of different income levels to the proportional number of families in each income level. Fourteen percent of the loans sampled were originated to low-income individuals. Thirty-two percent of all families within the bank's assessment areas are low-income. The bank's loan distribution to low-income individuals is reasonable given 34% and 30% of the families living in Harlan and Estill counties, respectively live below the poverty level. This high poverty rate is an indication that a significant number of families lack sufficient income to purchase a home. Thirty percent of the loans sampled were originated to moderate-income individuals. This distribution is reasonable when compared to the percentage (17%) of moderate-income families within the bank's assessment areas.

Table 6 Distribution of Residential Real Estate Loans by Borrower Income Level						
Income Level	Families in Assessment Areas		Number of Loans		Dollar Amount of Loans	
	#	%	#	%	\$ (000's)	%
Low-Income	4,589	32%	4	14%	\$34	5%
Moderate-Income	2,522	17%	9	30%	196	26%
Middle-Income	2,580	18%	6	20%	138	18%
Upper-Income	4,793	33%	10	33%	335	44%
Not Available	0	0%	1	3%	53	7%
Total	14,484	100%	30	100%	\$756	100%

Source: 1990 Census Data - U.S. Bureau of the Census and bank provided information

Small Business Loans

The distribution of small business loans by loan size is reasonable. Sixteen of the twenty-five small business loans sampled had original loan amounts of less than \$25,000. This indicates the availability of small dollar business loans in response to identified credit needs. HNB also has a reasonable distribution of loans by business revenue size. Fifty-five percent (11) of the small business loans (20) with revenue information were made to businesses that had gross revenues of less than \$100,000.

Consumer Loans

Table 7 compares HNB's consumer lending to borrowers of different income levels to the proportional number of families in each income level. Twenty-three percent of the loans sampled were originated to low-income individuals. This penetration is reasonable when compared to the percentage of low income families (32%) and the poverty rate noted above.

Twenty-three percent of the loans sampled were also originated to moderate-income individuals. This distribution is reasonable when compared to the percentage (17%) of moderate-income families within the bank's assessment areas.

Table 7 Distribution of Consumer Loans by Borrower Income Level						
Income Level	Families in Assessment Areas		Number of Loans		Dollar Amount of Loans	
	Number	Percentage	#	%	\$ (000's)	%
Low-Income	4,589	32%	7	23%	\$17	8%
Moderate-Income	2,522	17%	7	23%	23	12%
Middle-Income	2,580	18%	3	10%	6	3%
Upper-Income	4,793	33%	8	27%	122	62%
Not Available	0	0%	5	17%	30	15%
Total	14,484	100%	30	100%	\$198	100%

Source: 1990 Census Data - U.S. Bureau of the Census and bank provided information

Geographic Distribution of Loans

- **HNB’s geographic distribution of residential real estate, small business, and consumer loans reflected reasonable penetration throughout moderate-income geographies. We did not identify any conspicuous gaps in the penetration of geographies within the bank’s assessment areas.**

Residential Real Estate Loans

Table 8 compares the bank’s level of residential real estate loans to the proportionate percentage of owner occupied housing units by type of geography. Seventy-seven percent of the loans sampled were originated in moderate-income geographies. This penetration is reasonable when compared to the percentage (53%) of owner occupied housing units in moderate-income geographies.

Table - 8 Geographic Distribution of Residential Real Estate Loans						
Geography Income Level	Owner Occupied Housing by Geography		Number of Loans		Dollar Amount of Loans	
	#	%	#	%	\$ (000's)	%
Low-Income	0	0%	0	0%	\$0	0%
Moderate-Income	7,011	53%	23	77%	561	74%
Middle-Income	5,930	44%	6	20%	155	21%
Upper-Income	440	3%	1	3%	40	5%
Total	13,381	100%	30	100%	\$756	100%

Source: 1990 Census Data - U.S. Bureau of the Census and bank provided information

Small Business Loans

Table 9 compares the bank’s level of small business loans to the proportionate percentage of businesses by type of geography. Forty percent of the loans sampled were originated in moderate-income geographies. This penetration is reasonable when compared to the percentage (47%) of businesses in moderate-income geographies.

Table - 9 Geographic Distribution of Small Business Loans						
Geography Income Level	Businesses by Geography		Number of Loans		Dollar Amount of Loans	
	#	%	#	%	\$ (000's)	%
Low-Income	0	0%	0	0%	\$0	0%
Moderate-Income	404	47%	10	40%	317	31%
Middle-Income	357	41%	13	52%	613	60%
Upper-Income	108	12%	2	8%	98	9%
Total	869	100%	25	100%	\$1,028	100%

Source: Dun & Bradstreet, Inc. and bank provided data

Consumer Loans

Table 10 compares the bank’s level of consumer loans to the proportionate number of families by the type of geography. Forty-three percent of the loans sampled were originated in moderate-income geographies. This penetration is reasonable when compared to the percentage (54%) of families residing in moderate-income geographies.

Table 10 Geographic Distribution of Consumer Loans						
Geography Income Level	Families by Geography		Number of Loans		Dollar Amount of Loans	
	#	%	#	%	\$(000's)	%
Low-Income	0	0%	0	0%	\$0	0%
Moderate-Income	7,835	54%	13	43%	124	63%
Middle-Income	6,157	43%	17	57%	74	37%
Upper-Income	492	3%	0	0%	0	0%
Total	14,484	100%	30	100%	\$198	100%

Source: 1990 Census Data - U.S. Bureau of the Census and bank provided information

Response to Complaints

No complaints were received since the prior examination.

FAIR LENDING REVIEW

No violations of the substantive provisions of the anti-discrimination laws or regulations were identified.