



Comptroller of the Currency
Administrator of National Banks

SMALL BANK

Public Disclosure

October 22, 1998

Community Reinvestment Act Performance Evaluation

**The Honesdale National Bank
Charter Number: 644
733 Main Street
Honesdale, PA. 18431**

**Office of the Comptroller of the Currency
Northern Pennsylvania Field Office
100 Hazle Street, Suite 202
Wilkes-Barre, Pennsylvania 18702**

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 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 Honesdale National Bank** prepared by **The Office of the Comptroller of the Currency**, the institution's supervisory agency, as of **August 31, 1998**. This agency evaluates performance in assessment area(s), as they are delineated by the institution, rather than individual branches. This assessment area may include visits to some, but not necessarily all of the institution's branches. The agency rates the CRA performance of an institution consistent with the provisions set forth in Appendix A to 12 CFR Part 25.*

Institution's CRA Rating: This Institution is rated **SATISFACTORY**.

The primary factors supporting the bank's overall rating include:

- Lending levels reflect more than reasonable responsiveness to the credit needs of the community. An average loan to deposit ratio of 69% combined with a sizable mortgage servicing portfolio supports this determination;
- A majority of the HMDA, small business, and small farm loans originated during the evaluation period are within the bank's assessment area;
- The geographic distribution of loans originated during the evaluation period reflects reasonable dispersion throughout the assessment area.
- HMDA, small business, and small farm loans originated during the evaluation period are reasonably distributed among borrowers of different income levels and businesses of different sizes.

The following table indicates the performance level of **The Honesdale National Bank** with respect to each of the five performance criteria.

SMALL INSTITUTION ASSESSMENT CRITERIA	THE HONESDALE NATIONAL BANK 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 Businesses of Different Sizes		X	
Geographic Distribution of Loans		X	
Responses to Customer Complaints	No complaints about performance in meeting assessment area credit needs were received during the evaluation period.		

Description of Institution

The Honesdale National Bank (HNB) is the principal subsidiary of its holding company, Honat Bancorp, Inc. HNB is a retail community bank headquartered in Honesdale, the Wayne County seat, located in northeastern Pennsylvania. The bank operates four full service offices positioned throughout sections of Wayne, Lackawanna, and Susquehanna counties, and one mortgage production office in Luzerne County. Four of the bank's offices operate drive-up facilities and three MAC/Plus automated teller locations are maintained. The loan production office in Wilkes-Barre operates primarily

as a residential mortgage loan and student loan production facility. Two offices located in Montdale and Forest City, in Lackawanna and Susquehanna counties respectively, were opened since the last CRA examination. These offices were purchased from PNC Bank during 1996. No loans or deposits were included in the transaction.

Competition for loans is significant from Wayne Bank, The Dime Bank, and numerous community banks and offices of regional banks such as PNC, Mellon, and CoreStates. There are no known legal or financial factors that would impede HNB's ability to help meet the credit needs of its assessment area.

Since January 1, 1996, The Honesdale National Bank grew by \$41 million in assets to a bank with slightly more than \$181 million in total assets. Total loans outstanding at June 30, 1998 were \$111 million and investments totaled \$59 million at this date. Primary loan products include fixed and adjustable rate residential mortgages, small business and agricultural loans, and consumer installment, home equity, and student loans. The following chart illustrates the bank's loan portfolio distribution as reported in the June 30, 1998 Call Report:

Loan Portfolio Distribution at June 30, 1998		
Loan Type	Balance in (\$000)	% of Portfolio
Secured by 1-4 Family Residential Properties	39,745	36%
Consumer Loans to Individuals	19,898	18%
Construction and Land Development Loans	148	less than 1%
Commercial and Industrial Loans	49,606	45%
Secured by Farmland	462	less than 1%
Agricultural Production Loans	1,042	1%
Loans to Municipalities	569	less than 1%
Totals	111,470	100%

Description of Assessment Area

The Honesdale National Bank's assessment area (AA) meets regulatory guidelines and does not arbitrarily exclude any low- and moderate-income census tracts or block numbering areas (BNAs). The AA comprises 167 census tracts in the Scranton/Wilkes-Barre/Hazleton MSA 7560 and 20 BNAs in the non-MSA counties of Wayne and Susquehanna. Economic conditions in the AA are stable. Demographics of the area are highlighted in the following table:

Assessment Area Demographics

Characteristic	MSA 7560	Non-MSA	Combined MSA & Non-MSA
# of Census Tracts	167	20	187
% Low Income	1%	None	1%
% Moderate Income	13%	None	12%
% Middle Income	75%	100%	77%
% Upper Income	11%	None	10%
Population	547,188	62,037	609,225
Households:	212,823	22,892	235,715
% Low Income	1%	None	less than 1%
% Moderate Income	11%	None	10%
% Middle Income	75%	100%	77%
% Upper Income	14%	None	13%
Weighted Average of Updated Median Family Income	\$38,900	\$35,200	\$38,504
Weighted Average Median Housing Value	60,713	84,552	64,242
Total Housing Units	230,431	40,045	270,476

As indicated in the above table, thirteen percent of the geographies in the bank's AA

are low- and moderate-income (LMI) tracts. Each of these LMI census tracts are located in MSA 7560. HNB services this area through its branches in Montdale and Forest City, and its loan production office in downtown Wilkes-Barre. Seventy-seven percent of the combined census tracts and BNAs are middle-income tracts. The remaining ten percent are considered to be upper income tracts.

The projected population growth for the four county market area reveals a growth rate of (0.10%). Currently, 609,000 people live in the bank's AA, making up 235,000 households. Of these, 10% are identified as LMI households. The vast majority, then, are middle- and upper-income households. Income level comparisons are determined by the weighted average MSA/non-MSA's updated median family income, which for 1997 totaled \$38,504.

Management determines primary credit needs as residential housing, consumer credit, student loans, and small business and small farm loans. Our community contacts with two housing and redevelopment authorities operating within the AA corroborates the bank's determination.

CONCLUSIONS WITH RESPECT TO PERFORMANCE

Scope of Review: This review covered the time period from January 1, 1996 to August 31, 1998. All Home Mortgage Disclosure Act (HMDA), small business, small farm, and community development loans originated during this period were evaluated. Our loan review was assisted by bank management's compilation of data as required by the Community Reinvestment Act regulation. We also reviewed investments purchased and matured and services provided over the time period.

Loan-to-Deposit Ratio

HNB's loan-to-deposit ratio is more than reasonable, averaging 69% over the eleven quarter period ending September 30, 1998. The national peer group average for this same time period was slightly higher at 74%. Despite being lower than peer, HNB's loan-to-deposit ratio is strengthened by the bank's practice of originating and selling residential mortgage loans to the secondary market. During the examination period, HNB originated and sold \$69 million in residential mortgage loans to FannieMae and FreddieMac. The bank retains the servicing rights to 50% of these loans. As a result, the volume of originations and servicing portfolio is greater than the average loan-to-deposit ratio suggests.

Lending in the AA

As indicated by the table that follows, HNB demonstrates appropriate responsiveness to satisfying the credit needs within its AA. The following table identifies the HMDA, small business, and small farm loan originations by number and dollar amount.

Loan Originations in the AA from 1/1/96 to 8/31/98				
Loan Type	# of Loans	%	Amount of Loans \$(000)	%
HMDA Loans Originated in AA	803	66%	54,048	76%
Total HMDA Loans Originated	1,222	100%	71,415	100%
Small Business Loans Originated in AA	233	100%	14,088	100%
Total Small Business Loans Originated	233	100%	14,088	100%
Small Farm Loans Originated in AA	53	100%	1,561	100%
Total Small Farm Loans Originated	53	100%	1,561	100%
Total HMDA, Small Business, and Small Farm Loans Originated in AA	1,089	72%	69,697	80%

On a combined basis for the review period, the number of HMDA real estate mortgages, small business loans, and small farm loans originated in the AA averaged 72%. This correlates to an average of 80% of the total dollar volume of these same types of loans originated within the AA. This means that a majority of the HMDA real estate, small business, and small farm loans originated during the examination period were made within the bank's AA.

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

HNB has a good record of lending to borrowers of all income levels and to businesses of different sizes. The following table shows the distribution of the number and dollar volume of all HMDA residential mortgage loans originated during the evaluation period compared to the distribution of households of different income levels located within the AA.

The table reveals that HNB's lending to LMI borrowers is proportionately greater than the percentage of such households residing in the bank's AA. Over the evaluation period, 29% by number of the HMDA loans HNB originated and 20% by dollar volume were to LMI borrowers. This compares favorably to the AA's number of LMI households.

Total HMDA Loans Originated within the AA by Level of Borrower Income from 1/1/96 to 8/31/98					
Borrower Income Level	# of Loans originated	%	\$ Volume of Loans (000)	%	% of Households by Income Level Residing in the AA
Low	47	6	1,704	3	<1%
Moderate	186	23	9,128	17	10%
Middle	308	38	19,767	37	77%
Upper	262	33	23,449	43	13%
Total	803	100%	54,048	100%	100%

The following table further breaks down HMDA loan originations over an annual and year-to-date period to show that HNB's lending performance is consistent over the eleven quarter evaluation period.

Of the HMDA loans originated during 1997-98, 339 loans totaling \$19.5 million were made in conjunction with the Pennsylvania Housing Finance Assistance Agency. These loans enhance credit opportunities for LMI applicants by providing reduced interest rates and closing costs to qualifying borrowers.

Trend in HMDA Loan Originations within the AA by Level of Borrower Income				
	% of Loans Originated by \$ Amount During Examination Period			
Borrower Income Level	1996	1997	1/1/96 to 8/31/98	% of Households by Income Level Residing in the AA
Low	2%	3%	5%	<1%
Moderate	13%	22%	14%	10%
Middle	43%	35%	32%	77%
Upper	42%	40%	49%	13%
Total	100%	100%	100%	100%

The origination of HMDA loans over the evaluation period is distributed proportionately to the number of households of different income levels residing in the AA. The results indicate that HNB's lending to low-, moderate-, middle-, and upper-income borrowers is reasonable based on the income demographics of the households within the area.

Geographic Distribution

Home Mortgage Lending

HNB's AA includes two low-income census tracts and twenty-one moderate-income tracts. Together, these LMI tracts represent 12% of the bank's total geographies. The majority of housing in LMI areas consists of multifamily and rental units. Therefore, the inventory of housing for purchase in these areas is minimal and the opportunity to originate HMDA loans is limited. Owner-occupied housing in the low-income tracts is less than 1%, and only 6% in the moderate-income tracts. HNB's lending in its LMI census tracts averaged 7%. This activity compares proportionately to the percentage of owner-occupied housing available in these tracts.

The following two tables illustrate HNB's origination of HMDA mortgage loans compared to the income level of the census tracts making up its AA and the percentage of owner occupied housing by tract.

The table below reveals that HNB's origination of HMDA loans in LMI census tracts is proportionate to the volume of LMI tracts and the percentage of owner occupied housing included in the bank's AA.

Total HMDA Loans Originated in the AA by the Income Level of the Census Tracts from 1/1/96 to 8/31/98						
Borrower Income Level	# of Loans Originated	%	\$ Volume of Loans (000)	%	% of Tracts by Income Level	% of Owner Occupied Housing
Low	1	<1	76	<1	1%	<1%
Moderate	71	9	3,635	7	11%	6%
Middle	597	74	38,618	71	77%	80%
Upper	134	17	11,719	22	11%	14%
Total	803	100	54,048	100	100%	100%

The following table shows that HNB's trend in HMDA loan originations in the LMI census tracts is consistent over the evaluation period.

Trend in HMDA Loan Originations within the AA by the Income Level of the Census Tracts					
	% of Loans Originated During Examination Period				
Income Level	1996	1997	1/1/98 to 8/31/98	Total	% of Census Tracts by Income Level
Low	0	0	<1	<1	1%
Moderate	8	5	9	7	11%
Middle	71	72	70	71	77%
Upper	21	23	21	22	11%
Total	100	100	100	100	100%

Small Business and Small Farm Loans

The CRA regulation indicates that loan size generally correlates to the income size of the business and farm borrower. The regulation provides that if income data is not collected for certain loan types, an analysis by loan size could be used as a proxy to determine the income or revenue level of a borrower. Business and farm loans originated for amounts of \$1 million dollars or less, therefore, are considered to be made to small businesses and small farms. The following table shows the volume of small business and small farm loans originated during the evaluation period.

Small Business and Small Farm Loans Outstanding at June 30, 1998						
Original Amount of Loan	Small Business			Small Farm		
	# of Loans	\$ (000)	% to Total \$	# of Loans	\$ (000)	% to Total \$
< than \$100 thousand	191	4,524	33%	48	951	61%
\$100 to \$250 thousand	33	4,999	35%	5	610	39%
\$251 thousand to \$1 million	9	4,564	32%	0	0	0%
Total Commercial & Farm Loans	233	14,087	100%	53	1,561	100%

During the evaluation period, HNB originated no loans in excess of \$1 million dollars. The above table shows that, regarding loan size as a proxy, 100% of the commercial and agricultural loans originated during the evaluation period were made to small businesses and small farms. This translates into very good lending performance to these borrowers by HNB.

HNB actively supports the Wayne County Habitat for Humanity. The bank extended a \$20 thousand dollar line of credit at a zero percent interest rate to this organization. The loan is included in the above small business loan totals.

Responses to Complaints

HNB received no complaints regarding its performance in meeting the credit needs of its AA over the evaluation period.

Fair Lending Review

A fair lending review performed in conjunction with this CRA examination did not identify any violations of anti-discrimination laws and regulations. We noted no instances where HNB discouraged or impeded potential borrowers from applying for credit.

Investments and Services

Qualified Investments

Under the new CRA regulation, financial institutions can receive positive consideration for making “qualified investments.” A “qualified investment” is defined as a lawful investment that has community development as its primary purpose and benefits the bank’s AA. Community development investments provide affordable housing, community services, and activities that promote economic development in the LMI communities of the bank’s AA.

Qualified investments in HNB’s AA are limited and competition among financial institutions for such investments is strong. As a result, HNB made no qualified investments over the evaluation period. The availability of qualified investments and opportunities for future purchases were discussed with management. HNB is willing to explore avenues for the future purchase of qualified investments.

Services

HNB’s record of providing accessible branch offices, ATMs, loan production offices, and other services enhances credit availability in its AA. HNB operates four full service branch facilities with hours tailored to customer demand. Extended weekly and Saturday lobby and drive-up hours are offered to provide customer convenience. The loan production office in Wilkes-Barre offers evening and weekend hours by appointment.

HNB also operates three MAC/PLUS ATMs in the Honesdale area to facilitate customer transaction needs. Transaction services are provided through free checking accounts. Additionally, toll free customer telephone service is offered and an Internet website provides credit information and E-mail access.

Metropolitan Statistical Areas Conclusions with Respect to Performance Tests in MSA #7560

The Honesdale National Bank's performance in MSA 7560 - Scranton/Wilkes-Barre/Hazleton is consistent with the bank's overall lending performance. The bank identifies 167 census tracts within MSA 7560 as its AA. Only two tracts are identified as low-income tracts; tracts 1001 and 1002 located in the City of Scranton. Twenty one census tracts are designated as moderate-income, 144 are middle-income, and the remaining 19 are upper-income census tracts.

HNB services this MSA through three offices. During 1996, the bank purchased two full service branches in Montdale and Forest City from PNC Bank. These offices are located in the more rural regions of upper Lackawanna and southeastern Susquehanna counties. Although the Montdale office is included in MSA 7560, its location is distant from the more populated LMI census tracts in Scranton. Likewise, the Forest City office services upper Lackawanna, eastern Susquehanna, and upper Wayne counties which are rural and sparsely populated. Therefore, HNB's exposure from these two offices into MSA 7560 is limited.

The majority of loans originated by HNB in MSA 7560 are from its loan production office in downtown Wilkes-Barre, in Luzerne County. The MSA's population is 547,188, comprised of 212,823 households. Only 1% of the households in the MSA are determined to be low-income, with 11% being moderate-income. The Weighted Average Updated Median Family Income for MSA 7560 equals \$38,900.

Lending Test

HNB's origination of HMDA loans in MSA 7560 is illustrated in the following table. The table shows loan originations made within this MSA to borrowers of different income levels compared to the percentage of households residing in the MSA categorized by their levels of income.

During the evaluation period, approximately 20% of the HMDA loans originated by HNB were within MSA 7560. Of these, an average of 12% were made to LMI borrowers. This volume of originations is reasonable and proportionately representative of the demographics of the area. Both the number and dollar volume of HMDA loans originated to low- and moderate-income borrowers in this MSA are consistent with the 12% demographic averages of LMI households residing in the MSA. As a result, HNB exhibits good lending performance to LMI households in MSA 7560.

HMDA Loans Originated in MSA #7560 from 1/1/96 to 8/31/98					
Income Level of Borrowers	# of Loans Originated	%	Loans Originated \$(000)	%	% of Households Residing within MSA
Low	1	<1%	76	<1%	1%
Moderate	21	13%	1,241	12%	11%
Middle	104	66%	6,045	57%	75%
Upper	32	20%	3,182	30%	14%
Total Originated in MSA 7560	158	20%	10,511	19%	100%
Total Loans Originated in AA	803	100%	54,048	100%	NA

Scope of Examination	
Time Period Reviewed	January 1, 1996 through August 31, 1998
Financial Institution	The Honesdale National Bank
Products Reviewed	Mortgage, Small Business, and Small Farm
AAs	Scranton/Wilkes-Barre/Hazleton MSA 7560, and non-MSA areas of Wayne and Susquehanna counties
Type of Examination	On-site
Branches Visited	Main Office, Honesdale, PA